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Buyout: A Guide For Workers Facing Plant Closings

Office of Economic Policy, Planning and Research

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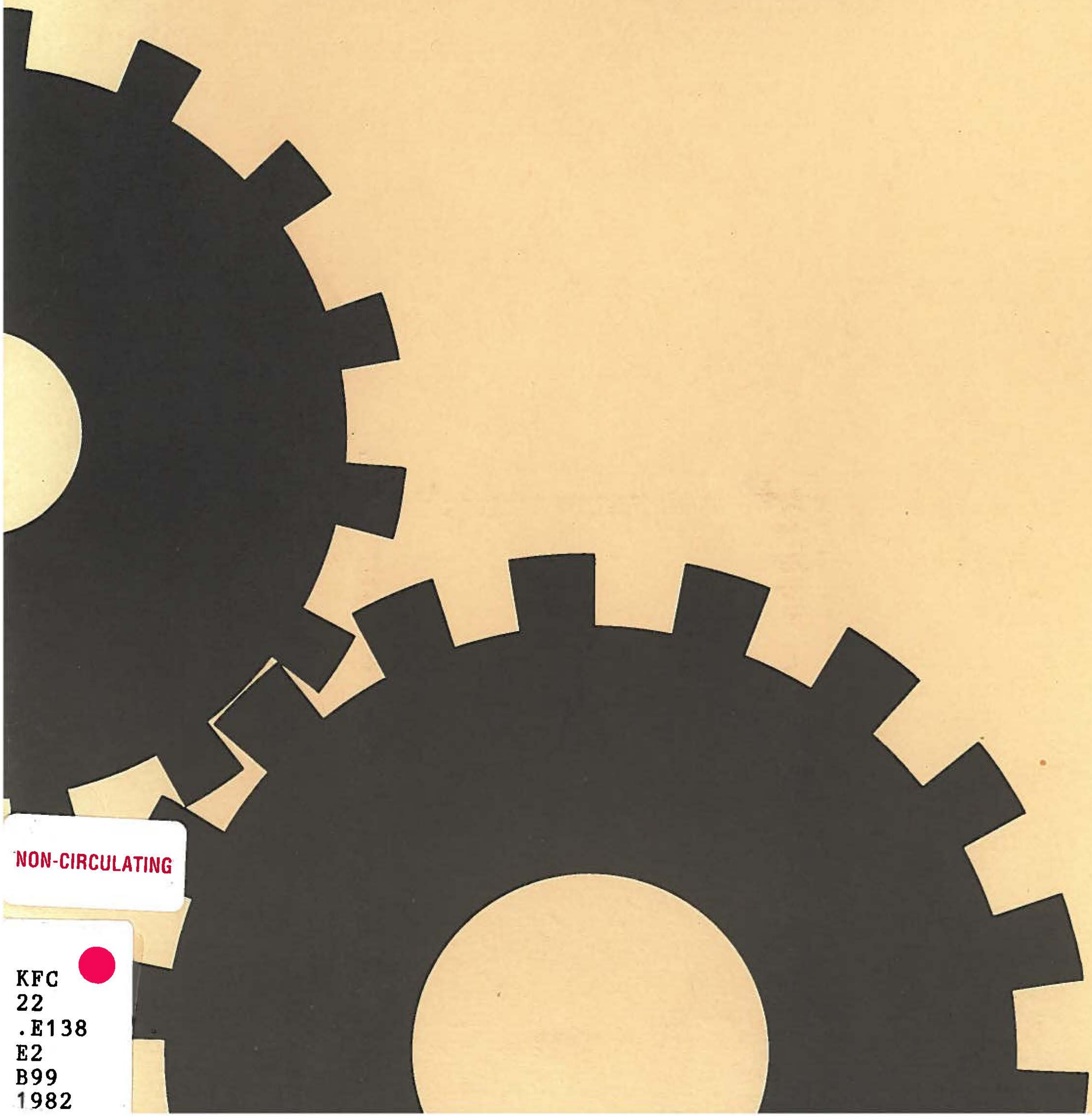

BUYOUT:

A GUIDE FOR WORKERS FACING PLANT CLOSINGS

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Office of Economic Policy, Planning and Research

in cooperation with

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U. S. WORKER BUYOUTS

* = Buyout

\+ = New company start-up

o = Buyout attempt

This list does not include companies sold to employees over time, such as the Milwaukee Journal, United Parcel Service, Graybar Electric Co.

INTRODUCTION

Every year hundreds of communities across the country face the problems of lost jobs and taxes when owners decide to close plants. **In most of these cases the plant closure is inevitable.**

Closing plants are not necessarily unprofitable, however. In some cases a branch plant may not fit into the parent company's overall business plans. In other cases, plants are closed because the parent company desires a greater return on equity. Plants also can close as the result of the death or retirement of the owner. Poor management decisions frequently cause businesses to decline. Some of these plants can be saved through employee ownership.

As plant closures have increased in number, labor unions have begun to reassess their choices in responding. New strategies to protect jobs and job rights often center on the need to involve members in corporate decision-making. It has become apparent that unions and workers can contribute to both improving company effectiveness and at the same time revitalizing communities. Workers and unions are now beginning to question whether they can afford not to have a more direct voice in business planning and decision-making.

In the past, when companies announced plant closures, unions had few options except to negotiate severance benefits or organize to persuade management to keep the plant open. **Increasingly, however, workers, unions, communities and government are seeking to avert closure by addressing the cause of the closing.**

Unions are also beginning to rethink their position on employee ownership. Until recently, most unions were skeptical about employee ownership and employee stock ownership plans (ESOPs). Despite this, ESOPs grew at a rapid pace during the 1970s, primarily in healthy companies. In addition, worker ownership has become another option to respond to plant closures.

In the last ten years, approximately 60 firms have been bought by local management and employees in response to potential plant closures. Stock ownership can mean influence over company policy, investment and direction. While concessions alone do not ensure any form of future gain to workers should the company improve, stock ownership permits workers to share in the future prosperity of the company.

Where workers own stock and have more direct input into management, the union can maintain its functions of collective bargaining, grievance handling, and contract administration. It also has greater input concerning the way problems are solved.

This booklet describes employee ownership as a response to plant closings and outlines issues of concern to unions. It can be used to help identify the feasibility of avoiding plant closures and preserving long-term jobs.

The appropriate alternatives to closure depend on the cause of the closure. In most cases, there is no choice but to close the plant. Examples include where there is a poor market for an undesired product, or where it is not feasible to produce a product competitively. For other causes, there are alternative solutions:

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Capital Scarcity: In addition to obtaining loans, loan-guarantees or government funding, employees can contribute to reducing costs or increasing capital by trading off benefits and targeting the traded funds for investment in stock, new technology, etc. (Examples: Pan American Airlines, Rath Packing Company, Morrell Company.)

High Production Costs: Plants can develop worker participation programs. Such labor input can reduce costs and increase productivity. Several unions have bargained for labor management committees. (Examples: Communication Workers of America and Bell Telephone System, United Steel Workers of America National Agreement, United Auto Workers with GM and Ford.)

Workers Compensation Costs: Union-Management Health and Safety Committees can improve the health and safety of workplaces, reducing accidents and insurance costs.

Energy Costs: Management can obtain an energy audit from the local utility company, free of charge. The audit identifies energy inefficiencies and suggests ways to reduce energy costs. The State of California, Department of Economic and Business Development, works with companies to develop cogeneration to save energy.

Current Product Is Not Viable: In some cases, new products with better markets can be produced using existing or similar production facilities. Employees can work with management as they did at International Silver in Connecticut to convert facilities to new businesses. (Examples: International Silver, International Association of Machinists.)

Plant Needs a Buyer: Closures can sometimes be prevented or their impacts reduced by sales to outside or local investors. In these cases, the community may help. (Examples: Clarksburg, West Virginia.)

The Plant Is Not a Good Fit With Conglomerate Parent: In some cases a plant may not fit into a conglomerate parent's overall plan. In other cases, the plant may not earn high enough profit for the conglomerate parent. (Example: Sperry Rand Corporation and the Library Bureau plant.) In a few cases, conglomerate management may not be well equipped to effectively manage a local company. (Example: Cluett Peabody and its Van Ralte knitting mill.) These are some of the more likely situations in which to investigate employee ownership.

If the causes of the potential closure can be removed, then employee ownership may be a viable alternative. In fact, in many recent situations involving the announcement of a plant closure, the feasibility of keeping the plant open is being at least cursorily investigated.

To assist unions in evaluating this option as a response to plant closings, this booklet is divided into two parts. The first part is an introduction to employee ownership that includes examples, approaches and a description of the union role in an employee owned company. The second part is a guide to investigating employee ownership including factors for success and the steps in preparing a feasibility study. Supporting materials, resource lists and a guide to organizing a buyout are included in appendices.

I. INTRODUCTION TO WORKER/EMPLOYEE OWNERSHIP

DESCRIBING EMPLOYEE OWNERSHIP

Employee ownership of business is one of the most rapidly growing phenomena in the American economy. **Almost unknown a decade ago, there are now approximately 5,000 employee ownership plans and about 500 companies where the majority of stock is owned by the employees.** Most of these are in profitable companies. Employee owned firms range from such diverse industries as newspapers (The Milwaukee Journal) to rail transportation (The Chicago Northwestern). The Record Factory and Brook's Camera and the Bay Area Scavenger Garbage Co-ops are large employee owned companies in California.

WORKER OWNERSHIP IN THE PAST

Worker ownership goes back to the 19th Century, when worker owned enterprises were called producer co-operatives. In the 1830s, workers formed worker co-operatives during strikes and lockouts. Unions were illegal but workers were craftsmen with their own tools and skills. During lockouts they started their own companies.

Producer co-operatives attained their greatest strength under the sponsorship of the Knights of Labor, the major organization of workers in the United States before the American Federation of Labor during the 1880s. By 1880 there were over 200 Knights of Labor Co-operatives, mostly started through local unions. These included grocery stores, banks, newspapers and factories.

Some of these co-ops lasted more than 20 years. Most failed, however, because of lack of capital, overzealous price-cutting, boycotts by business and the banks, or lack of confidence by the workers in running their own company. The coops that succeeded were often sold by the workers to anyone who could buy shares.

In the twentieth century, many of these examples of worker ownership have been largely unnoticed. For instance, there are over a dozen plywood cooperatives in the Northwest which have existed since the 1930s. They were born out of necessity when workers faced unemployment lines if they didn't buy their factories from their bankrupt employers. In over 30 towns, from the Puget Sound to Humboldt Bay, workers started up or reopened plywood mills under worker ownership and management. These companies, ranging in size from eighty to 450 workers, made up one-eighth of the Douglas Fir plywood industry in 1974.

EMPLOYEES BUY PLANTS TO SAVE JOBS

During the last fifteen years, there have been several waves of major conglomerate mergers. In some, the acquiring company found itself wi h factories or divisions it had little knowledge of or interest in. As the economy worsened in the last several years, these "misfits" have been among the first factories to be sold or shut down.

At the same time, drastically increased energy prices and fierce international competition have made many company's equipment and products obsolete.

As the number of plant closings increased in the late 1970s, many groups of workers and unions began to explore the use of employee ownership as a means to keep operating those factories which private investors were abandoning.

Increasingly, employees have come to realize that while the majority of plants that close are not viable, some plants close for reasons other than not making a profit, and a few unprofitable plants can be profitable.

This does not suggest, however, that employees should buy every company threatened with a shutdown. Most enterprises that close are no longer economically sound. Employee buyouts are still relatively rare given the thousands of plants that are shutdown in the U.S. each year. Each situation must be carefully examined on its own merits.

In spite of the difficult obstacles a buyout presents when it is even considered an option, employee ownership has been extremely successful. Employee ownership has saved at least 50,000 jobs directly, plus thousands more in businesses that depend on those revitalized enterprises. What is more impressive is that to the best of our knowledge only four employee buyouts, involving 300 employees, have failed.

RECENT EXAMPLES

There have been about 60 worker buyouts since 1971. The largest of these is now underway. National Steel in West Virginia is being bought by its 11,000 Independent Steelworker's union employees. **Below are some examples in which employees purchased companies to save jobs.** More detailed information on effective ownership structure and worker involvement in these companies can be found in Factors for Success, pages 17-26.

Chicago Northwestern Railroad: In 1972, one of the first and largest employee owned companies was bought by employees for $30 million while the parent, Northwest Industries, claimed a tax loss of $200 million. The company, long in the red, earned profits in most of the years following its purchase by railroad employees. Worker owners stock increased greatly in value, it gained $3.89 per share in 1981. The railroad is currently in a major expansion program to invest in technology while reducing fuel and other costs through a worker suggestion program.

Vermont Asbestos Group: America's only worker owned mine was a heavy duty ore extraction operation that sold $7 million worth of asbestos fiber annually. Bought in a merger by GAF Corporation, the Vermont mine was about to be liquidated in 1975 because of low ore prices, depletion of the mine's resources and potentially heavy regulation costs. Local residents and the 198 workers attempted several tactics to block the firm's closure and eventually turned to worker ownership as a last resort. Miners collectively set up an ownership plan and sold shares for $50 each. The average amount of shares purchased was $300 paid for by workers and/or residents in the community. With $100,000 raised in cash contributions for stock, a consortium of 7 banks agreed to loan $1.5 million to the firm. The parent corporation, GAF, also loaned the new company $250,000 and agreed to sell the plant at a reasonable price of $400,000.

A board of directors, including union and management representatives, was established. In the first year asbestos increased in price 65 percent and workers' $50 shares increased in value to $2,000 per share. The company also made greater profits as a worker owned firm, since maintenance and repair costs were reduced. Recently, many workers sold these shares at a great profit and now outside investors control the once worker owned mine.

Saratoga Knitting Mill: One year later in New York, a knitting mill was being sold by a conglomerate. The mill, which produced women's lingerie, had been losing money. Conglomerate management had adversely affected sales since it had eliminated the mill's sales department. In the year after the employee purchase, the value of stock went up and revenues were constant even though the textile industry was experiencing difficulties. The company continues to be profitable after six years of worker ownership. During the 1982 recession, SKM was running at 40 percent capacity. However, the company seeks to develop new products to ensure company success.

Library Bureau: Nearby in Herkimer, New York, a wooden library furniture factory was bought by employees and the community in 1976. The Library Bureau was founded in 1876 but had been owned by a conglomerate, Sperry Rand, for 20 years. In 1976, the parent firm announced the Library Bureau was not making the 22 percent profit that headquarters required. The firm was to be closed and all 270 workers would be without jobs.

Such a shutdown would be devastating to an area already suffering from nearly 14 percent unemployment, so a plan was laid to buy out the owners and salvage as many jobs as possible. Within seven months $4 million was obtained from bank and government loans. An additional $1.8 million was raised from the sale of stock in the new company, Mohawk Valley Community Corporation. Over 3,500 people bought stock and the firm became owned by workers, managers and area residents.

South Bend Lathe: In 1975, Amsted Industries, an absentee owner, decided to shut the doors on its 70-year old plant in Indiana. The plant's 500 employees were shocked that their $20 million business which produced lathes, drills and presses would cease to exist. An ESOP was established with a $5 million federal Economic Development Administration (EDA) loan to the city, which in turn loaned the capital to the workers' trust. Another two million dollars was loaned by banks and the new firm was launched.

South Bend Lathe's profits dramatically improved under worker ownership. In the first month scrap diminished by 70 percent. As part of the Amsted conglomerate, the firm had sustained heavy losses in its last five years. Now worker owned, sales rose by 53 percent, productivity was up by 25 percent and after tax profits grew to over a million dollars for the first year. Although workers struck their own company in 1980 (see Effective Ownership Structure and Worker Participation, pages 23-25 for details), the plant continues to be profitable after seven years of worker ownership.

Rath Packing: In 1979, 2,300 workers were faced with demands for concessions to attract investors necessary to save the failing company and to obtain government funding. The union led the efforts to save jobs. Instead of providing concessions and stepping outside of the United Food and Commercial Workers (UFCW) master agreement, Local 46 members proposed remaining in the master agreement and deferred wages to buy Rath stock. Stock bought with employee wage deferrals was used as match money to leverage a Federal/Urban

Development Action Grant (UDAG) loan. Employees now own a controlling interest in the company. Deferred benefits will be paid back to workers in a pre-tax profit sharing plan that gives employees 50 percent of the profits. The union also negotiated for the power to appoint 10 new members to the existing six member board of directors, providing the union with majority control.

Rath made $3.3 million during the first year of employee ownership. Rath did well compared to other packing companies. In contrast to most in the industry, Rath increased its sales volume. Worker ideas and input in 1981 resulted in productivity and yield gains of more than $2.5 million. Absenteeism was reduced by 50 percent in the last year. Employees come in on their own time before work to discuss problems and seek information. In 1982, the company was still troubled. Both declining demand and restructuring within the industry contributed to net losses. In spite of this, union and management work to return the firm to profitability. The union assists other unions and groups of workers who visit Rath to learn how they too can respond to plant closings by buying their company.

Hyatt Clark Industries, Inc.: General Motors planned to close their Clark, New Jersey plant. The facility which produces roller bearings, is outdated now that the industry has turned to front wheel drive. A coalition of managers and leaders of Local 736 U.A.W. responded to the closing by offering to purchase the plant in the fall of 1981. After considerable negotiation, General Motors not only agreed to sell its operation, but to help finance the deal and purchase its output for the next three years. GM received $30 million in cash, $10 million in non-voting stock and provided $13 million in loans. In addition, several banks and insurance companies helped finance the buyout. Workers deferred 30 percent of their wages (from $13.40 to $10.40/hour), however, an incentive system based on productivity boosts monthly earnings. As loans are paid off stock reverts to the company so that within 10 years the company will be fully worker owned.

The union insisted that company stock be divided equally among all employees. Shares are held in a trust and can be sold only upon leaving the company. The two UAW leaders administer the pension program. In addition, they sit on the company board of directors along with a third union appointed member, three representatives from management, and seven outside directors.

Workers have input on all levels of the company through labor management committees. Initial results are positive. The workforce is up 30 percent to 1,100 employees. The company runs effectively with less than half the management that was required under GM's direction. The union has currently begun to study new products which the firm could produce once the demand for rear axle bearings declines in the next decade.

Capitol City Co-op: In Sacramento, a cabdriver co-op formed in 1982 during a strike by a SEIU local against Yellow Cab. The 40 cab drivers ended the cab monopoly in the city and invested $63,000 to buy 10 cabs and began a worker owned, worker run, unionized cab company. The Cab Co-op is modeled after Denver's Yellow Cab Co-op, which is based on the principle of one person/one vote. The two cab co-ops continue to cooperate and exchange information.

SOME EFFORTS TO BUY PLANTS ARE UNSUCCESSFUL

Cases where workers successfully purchased their plants do not suggest that employees can buy every company threatened with a shutdown. Many enterprises are no longer economically sound. In other cases workers cannot obtain funding, the former owner will not sell or other problems arise. Buying a company is complex. Some of the employee ownership attempts which have not succeeded are described below.

Colonial Press: Colonial Press in Clinton, Massachusetts was owned by a single family for over 30 years and had generally experienced steady growth. In 1967 it was sold to another corporation which was acquired by Sheller-Globe in 1974. The management of Sheller-Globe had no experience in the book industry. They failed to modernize equipment and charged the Press $900,000 a year for corporate overhead. Colonial Press had been losing money for two years when, on March 17, 1977, they announced plans to sell or liquidate the company.

With the assistance of the American Friends Service Committee for Economic Alternatives, a group attempted to buy the Press and form a worker cooperative. Within four days, 600 workers had pledged $400,000. At first, Sheller-Globe seemed likely to sell the Press to the workers as a going concern. Later they decided it was more advantageous to take a larger loss for tax purposes and the plant was liquidated.

With the assistance of the Industrial Cooperative Association (ICA) and the National Consumer Cooperation Bank, some former employees were able to start a new company, the Colonial Cooperative Press. This new firm was only able to employ about 30 of the original 750 workers, and soon failed.

Youngstown Sheet and Tube: In 1969 the Lykes Corporation acquired a much larger firm, Youngstown Sheet and Tube Company (YST). Lykes executives were more interested in expanding non-steel activities than in keeping steel facilities up to date. As a result, earnings dropped to the break even point and a decision was made to close down the Campbell Works rather than spend $500 million to modernize.

The "Ecumenical Coalition of the Mahoning Valley" was created and led a drive to reopen the mill. More than $4 million was raised as other groups and United Steelworkers Local 1462, gradually responded to the clergy's initiative. The campaign attracted national attention through television and press coverage.

A $300,000 grant was awarded by the U.S. Department of Housing and Urban Development to finance a feasibility study. Churches and synagogues contributed another $450,000. One third of the new firm was to be owned by a community development corporation (CDC), one third by an employee stock ownership plan (ESOP) and the remaining third would be owned by private investors. Each group would select a third of the board of directors (BOD).

The plant never reopened. Lykes merged with another conglomerate LTV, which already owned Jones and Laughlin Steel Corp. (J&L). Since the proposed plant would be in direct competition with LTV's other interests, they refused to cooperate in the sale of the Campbell Works to the coalition. The final blow came in April, 1979 when the Economic Development Authority (EDA) announced it could not provide the $245 million loan guarantee needed by the coalition to reopen the plant. Since the steel industry is now operating at less than half of capacity due to the extended recession, the newly worker owned company would have faced severe difficulties soon after reopening.

<u>Pueblo Packing Company</u>: Alpha Beta grocery stores closed the Pueblo Colorado Packing Plant in early 1981. Workers, union and community mobilized to save the plant. The State of Colorado provided technical assistance to the buyout attempt and the group hired a private firm to conduct an $80,000 feasibility study. Unfortunately the feasibility study included large errors, affecting potential bank investors and preventing employees from obtaining funding for the buyout.

<u>Circle Packing Company</u>: Employees in East St. Louis, found that funding was difficult to obtain to reopen the aging packing house once it had closed. The group hired a general manager to meet National Consumer Coop Bank requirements for a loan; however, the bank then refused the loan for other reasons.

At the <u>New York Daily News</u> in New York City and the <u>Butler Mining Company</u>, employees and union made crucial errors in timing which thwarted buyout efforts. In both cases a group organized to buy the company; however, reports that a new buyer had been found for the facility stalled further activity toward an employee purchase. The employees preferred to "wait and see" if a buyer could be found. After several months, when the potential buyers disappeared, the plants were due to be closed and employee/union groups had lost the necessary preparation time to initiate a buyout.

FORMS OF EMPLOYEE OWNERSHIP

The form of employee ownership that is best for one plant might not be best for another. **Many factors such as type of production, cohesiveness of the workers and community, and worker goals influence decisions on what the form of ownership will be.** The overall advantages and disadvantages of worker ownership are described in Table 1.

In the U.S. there are two predominate legal structures used in employee ownership. Employees can incorporate as a co-operative or they can buy a majority of the firm's stock through an Employee Stock Ownership Plan (ESOP).

WORKER CO-OPERATIVES

The co-operative form of ownership has several basic characteristics. **Co-operative elements include: only one share can be owned per member; all owners have the right to work in the co-operative; and all shares have one vote.** These characteristics make a co-op ownership structure automatically democratic, unlike ESOP ownership, which can be structured in a variety of ways.

Essentially, a co-op begins when each member buys one share. Co-operative laws put a limit on the allowed return on investment to stockholders. In California that limit is 5% on par value of the stock per year. Most co-ops prohibit payment of dividends. Profits are shared through a "patronage" refund to workers based on the number of hours worked or gross pay. Wages vary according to skill and seniority.

Worker co-operatives in California generally incorporate under Title I, Division 3, Section 12200 of the California Corporations Code. Most co-ops are small with less than ten employees. Producer co-operatives primarily exist in California agriculture.

There are thousands of worker owned co-operatives in the United States. Most are small shops, restaurants or retail outlets but some are larger firms. Some of the oldest and most successful are the plywood co-operatives of the Pacific Northwest.

ESOPs

An Employee Stock Ownership Plan (ESOP) is a benefit plan for employees, a financing vehicle with major tax incentives and a means to establish employee ownership. There are about 5,000 ESOPs in the United States. About 500 of the companies are majority owned by employees. According to the ESOP Association of America, California has more ESOP firms than any other state. Majority ESOPs are increasing in California as retiring owners sell their firm to employees.

An ESOP is similar to a profit sharing plan or a pension plan with two major differences. In the first place, the ESOP is designed to invest solely in the stock of the employee's corporation for the benefit of employees. In addition, the ESOP is permitted to borrow money to purchase employer stock.

ESOPs have been the most common financing structure for employee buyouts. In an ESOP buyout, an ESOP trust is established, either in the existing firm or in

Worker owners at the Solar Center in San Francisco mount solar collectors on buildings throughout the San Francisco Bay Area.

Table 1

ADVANTAGES AND DISADVANTAGES OF EMPLOYEE OWNERSHIP

Advantages:

- Can permit employees to have greater control of their company and, sometimes, preserve their jobs.

- Can save jobs for communities by keeping a firm locally owned.

- Can provide company with good public relations since employees can purchase the firm and maintain their jobs when other buyers are not found.

- Allows existing ownership to divest itself of an unwanted subsidiary.

- Allows major shareholders in closely held corporations to transfer stock to employees.

- Stock ownership and profit sharing can stimulate employee motivation and, thereby, increase profitability. ESOP firms have been found to be more productive than comparable conventional firms.

Disadvantages:

- Workers could buy an undercapitalized business that is bound to fail.

- Even if the business is saved, failure to introduce worker input at all levels has often caused dissatisfaction and led worker owners to sell out to private investors.

- Union can begin to overemphasize management's concerns about profitability which may not always be consistent with worker interests.

a newly formed employee owned company. The trust normally borrows money to buy controlling interest or 100% interest in the new company. This may be done in a single transaction, as usually happens in a conglomerate divestiture, or over a period of years, as is common in the sale of closely held firms. The ESOP trust repays the loan when the ESOP company contributes an amount equal to each payment due on the loan into the ESOP trust. In return, shares of ownership are allocated to the workers (see Table 2). In many small businesses, conversion to employee ownership occurs when the company contributes cash to the ESOP trust and the trust buys company stock.

ESOPs have two general attributes not now available to co-ops. The first difference is that in general, ESOPs have had greater access than co-ops to traditional financing sources. This is in large part because financial institutions often lack familiarity with co-ops. Co-ops do not provide incentives to attract outside equity financing. In addition, ESOPs reduce the ESOP firms' taxes because principal and interest paid to the ESOP tax are deductible. This advantageous tax treatment for money raised through an ESOP* can make the new employee owned company better able to operate profitably. In addition, employee owners pay for their purchase in tax-exempt dollars, much like an Individual Retirement Account (IRA).

Employees can maintain control by requiring the ESOP to repurchase stock shares of employees leaving the company. Retiring employees can receive cash for their stock. Appreciation in investment can be treated as capital gains so that the income tax is less when the stock is converted to cash. The stock distribution could also be "rolled over" into an Individual Retirement Account (IRA) to defer taxes or it can be treated according to IRS rules for ten year averaging.

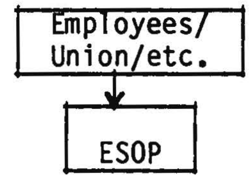
The differences between ESOPs and co-ops are summarized in Table 3.

* Further tax advantages can be obtained through a PAYSOP, which is similar to an ESOP, although the company can deduct its PAYSOP contribution from its tax payment.

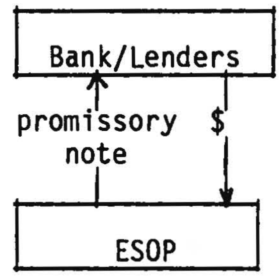
Table 2

HOW AN ESOP CAN BE USED TO SHIFT OWNERSHIP

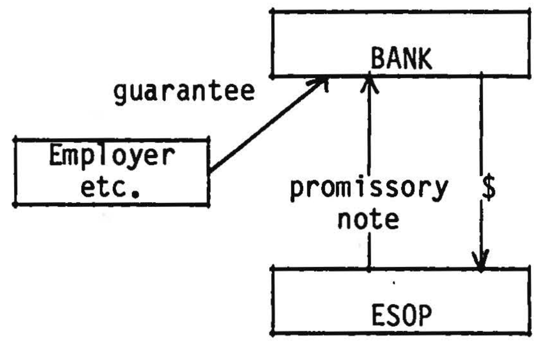
1. The existing owners, union or community organization sets up an ESOP to buy employer stock.



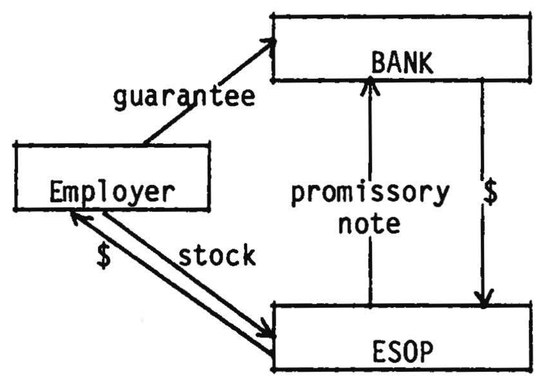
2. The ESOP borrows the balance of the purchase price from a lender or group of lenders such as employees, private parties, banks, city industrial revenue bonds, etc. ESOP signs a promissory note for the money.



3. Any of the interested parties may guarantee the loan or a portion of it.



4. The ESOP then uses money from the loan to buy stock from the existing owners.



5. The new company annually contributes enough cash to the ESOP to amortize the loan. The contribution is tax deductible.

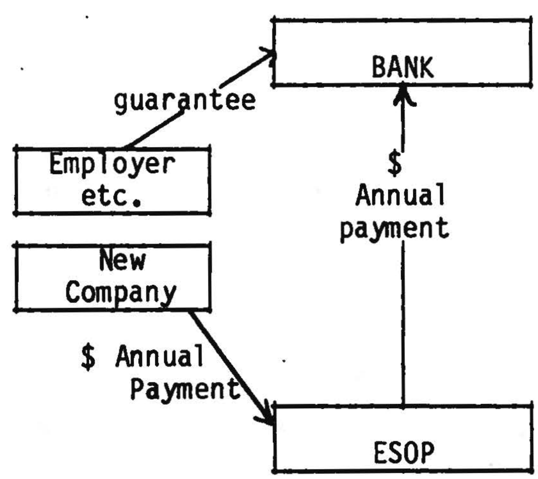


Table 3

ESOPs AND CO-OPS: WHAT ARE THE DIFFERENCES?

Co-op	ESOP
o A co-op begins when each member buys one share.	o In an ESOP buyout, an ESOP Trust is established, often to borrow money to buy the company.
o A co-op is a union of people to supply themselves with goods and services.	o An ESOP is a union of investors to earn a profit.
o Co-op structure is automatically democratic. In a co-op, all shares have one vote.	o ESOP structure can vary. Precautions must be taken to assure that employee owners have desired voting rights. Democratic ESOPs based on one person/one vote are established by creating a two-tiered ESOP structure. Employee owners, on a one person/one vote basis, instruct the ESOP trustees to vote the shares.
o In co-ops tax is paid either by the corporation (corporate tax) or by the member (personal income tax) in the year that the dividend is earned.	o Tax benefits are available to ESOPs which are not available to co-ops. ESOPs have a cash flow advantage over co-ops since the firm and employee owners both defer taxes until ESOP shares are finally distributed.
	o In a buyout, an ESOP reduces the new firm's taxes because the principal and interest paid to the ESOP are tax deductible.
o Because of the de-emphasis on the investor, co-ops are not able to attract equity investment as for-profit firms do: the incentive isn't there. Co-ops generally depend upon their own members for equity financing.	o ESOPs can help worker buyouts gain access to traditional lending institutions. o In a leveraged ESOP, workers become owners of stock paid for out of future earnings of their company.
o Co-ops can have lower transaction and maintenance costs than ESOPs.	o ESOPs are subject to ERISA laws which cover pension plans and include substantial legal reporting requirements.
o The co-op structure is most easily applied to 100% owned companies.	o ESOP ownership can apply to any amount of stock.
o Co-op return (patronage refund) is based on hours worked or gross pay. The role of the investor is de-emphasized.	o ESOP return (profit) is based on stock ownership or investment.
o Current California co-op law limits the return to 5% on par value of the stock per year.	o ESOPs have no limit to the return (profit) to employee owners.

THE UNION ROLE IN A WORKER OWNED COMPANY

The unions in worker owned firms can and do serve to protect the interest of workers as they do in traditionally owned firms.

David Ellerman of the Industrial Cooperative Association, describes the union role in an employee owned or co-operative firm as that of the loyal opposition. In a firm where employees have started a cooperative or purchased a traditionally owned firm, the union continues to provide "needed checks and balances on the daily exercise of power."

Companies which are democratically structured make worker input into decision-making possible. Even in these democratic firms, however, the union speaks for workers as a group to assure that the democratic structures are effective.

James Smith, Assistant to the President, United Steelworkers of America notes that:

> "Worker owners have two sets of interests, arising out of the separate roles of worker and investor...the need for unions in employee owned firms will continue, because workers will continue to perceive the need for them. **I certainly wouldn't fear for the future of the USWA if every employee in the United States became an ESOP company because workers will still need organizations** through which they can:
>
> 1. Inform themselves of the wages, benefits, etc. of others in their industry or trade;
>
> 2. Inform themselves of the true financial condition of their own employer, and assess the meaning of that financial condition in terms of their own interests as workers;
>
> 3. Negotiate with management for the protection or improvement of their standards of living, insurance, retirement income, etc.;
>
> 4. Negotiate and enforce equitable arrangements for promotion, demotion, layoff, recall, prevention of unfair discipline, the structure of wage relationships, and other working conditions problems;
>
> 5. Establish and enforce safe and healthful working conditions, and inform themselves on workplace hazards; and
>
> 6. Inform themselves of their own interests in the political and legislative processes of their community, state, and nation, and act collectively to pursue those interests."

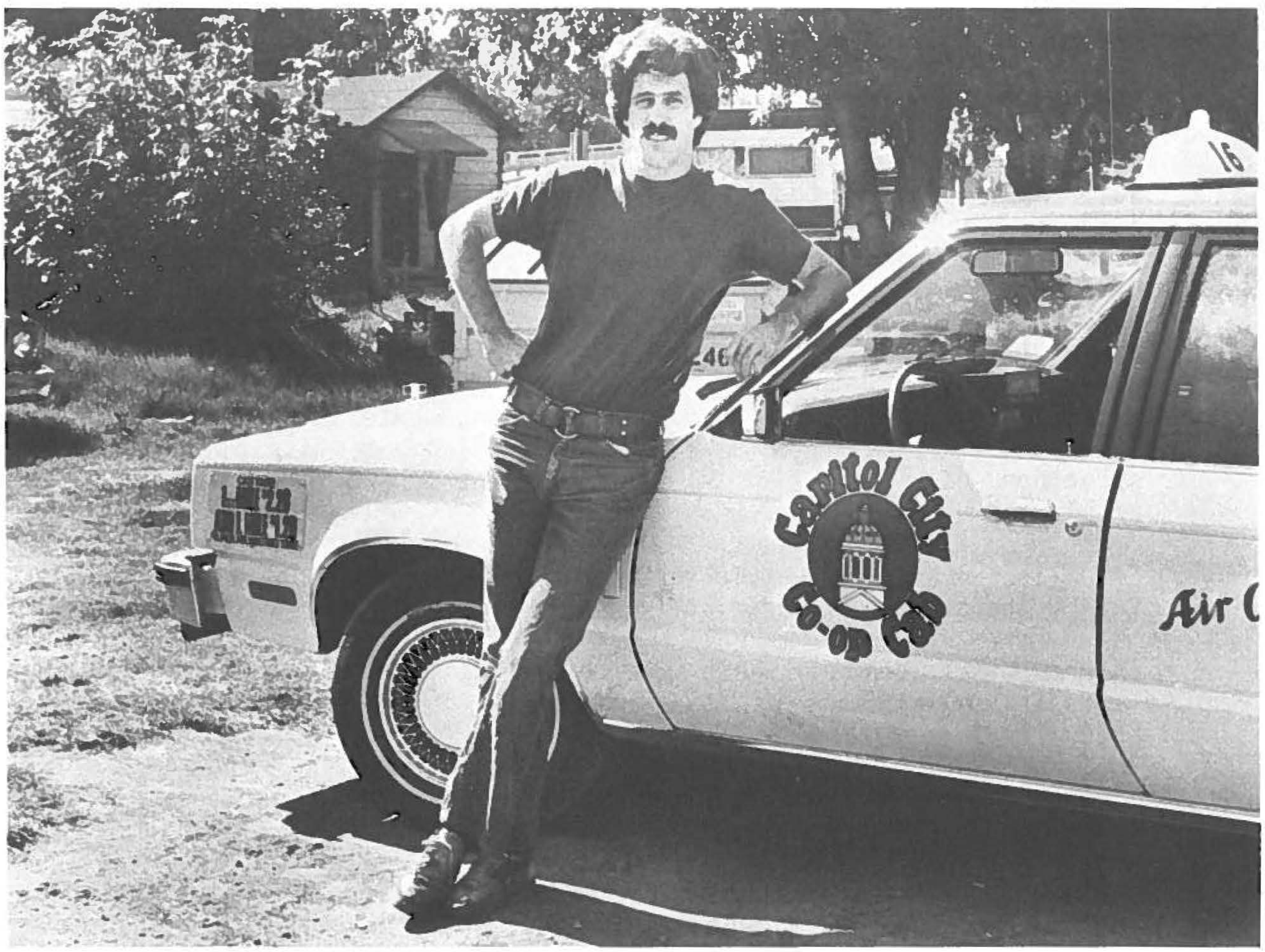
The union role remains very important. Stewards continue to handle grievances, and the union bargains with the board of directors at contract time.

The union role is enlarged. In addition to representing employee individual rights, the union can speak for workers as owners. In the worker buyout at Rath, for example, for the first two years the union served as a watchdog over management to assure that the company was managed in the interest of the worker owners. Union representatives became involved in suggesting changes in company policies on all levels of the company. This includes receiving information and reviewing raw material prices, sales strategies, marketing, methods, and investment.

Worker owners have two interests: to distribute profits in higher wages and to retain profits for reinvestment. A union in an employee owned firm must consider not just wages but also reinvestment in the firm. In some cases the union may take the position that reinvesting in the company rather than distributing higher wages is to the advantage of the worker owners.

Unions can lead the efforts to use the knowledge and skills of all employees. Recently for example, the union at Rath received a government grant to train Rath workers and supervisors in how to work together better in the new company. When worker participation is combined with worker ownership, improved communications between labor and management can increase productivity.

There is little evidence to suggest that employees do not feel the need for a union in an employee owned firm. Surveys at unionized employee owned companies suggest that most employees believe in each case that the union is necessary to protect worker interests.



In 1982, over sixty cab drivers formed a successful unionized cab co-op in Sacramento, California.

II. GUIDE TO INVESTIGATING EMPLOYEE OWNERSHIP

FACTORS FOR SUCCESS

Purchasing a company or plant is a difficult process. The experience of both successful and unsuccessful worker buyouts in recent years clearly indicates that certain factors increase the chances of success. The conditions are summarized in Table 4 below. However, even if all of the factors are present, success is not guaranteed. If a few of the factors are not present, it is still possible to create a viable worker owned corporation, although the path will be more difficult. For example, even though the Library Bureau received little advance notice to put together its successful buyout, employees were able to overcome this deficiency by mobilizing community, political, and management support.

This section describes in some detail the factors required for success by discussing the experience of previous buyouts and proposing specific actions which have been found useful in the past. The work described in this section can be done by a few individuals or by organizing much larger and more formal task forces. Either method can work; both approaches have succeeded and failed in the past. **The key point is that each of the factors for success is important and must be addressed. Appendix V, page 64, describes specific steps for organizing the effort to buy a plant, including a checklist of key issues to be addressed by a recovery committee.**

TIME

Time is critical to organize for the employee purchase, to obtain a feasibility study, create a business plan, obtain funding and negotiate with the former owner. **Enough time is needed to pull all of the pieces together before the plant closes, and before key customers and suppliers are lost.** A buyout can occur after a plant shuts down, but all of the difficulties are magnified. Once a plant closes, machinery can be removed and there can be substantial new costs to restart production. After the owners have liquidated the firm, obtaining information on economics of the firm becomes very difficult. After workers are laid off, union locals can disintegrate and, if this happens, there is no vehicle to mobilize workers for a buyout.

Once a decision supported by the employees to consider a buyout is made, the employees must organize quickly, and use a specific work plan. Firms rarely announce closures more than a few months before they occur. In contrast, just to put together an adequate business plan can take six months (one month for work plan, four months for feasibility assessment, and one month for business plan). If there is little time for preparation, then consideration of a buyout should hinge upon extremely good reasons for believing that the new venture will be successful.

EMPLOYEES AND COMMUNITY ARE MOBILIZED

The involvement of the employees and the community in organizing an employee buyout strongly affects both the probability for initial and long-term success. Key steps to consider in mobilizing the community can be found under "Public Information and Mobilization," Appendix V, page 67.

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Table 4

FACTORS FOR SUCCESS

- ☐ Time is available for response.
- ☐ The employees and community are mobilized.
  - ☐ The union is supportive.
  - ☐ The community is mobilized.
    - ☐ Elected officials
    - ☐ Local business
    - ☐ Labor
    - ☐ Churches
    - ☐ Grassroots
    - ☐ Media
- ☐ The firm to be purchased will be viable.
  - ☐ A market exists.
  - ☐ The plant can compete.
  - ☐ The plant can make a smooth transition away from any existing ownership (i.e., it has committed managers, necessary facilities, corporate functions, and market access).
  - ☐ The current owner is cooperative.
  - ☐ Financial backing is available.
- ☐ Technical assistance is available.
- ☐ The newly formed firm has a viable organizational structure.
  - ☐ Concerned parties agree on a structure.
  - ☐ Employees of the new firm will participate in all levels of decision-making.

Union Involvement: In the past decade unions have had varied responses to employee ownership attempts. In some cases they take a "wait and see" approach. In others, unions lead the effort to save jobs. Union involvement in initial organizing and structuring of employee ownership plans has a strong influence on success.

Wait and See:

Unions have often taken the wait and see approach toward alternative ownership when plants close. The approach provides for little involvement or input from the union in events leading to the buyout or in the structure of ownership proposed. Later, problems may develop when the situation isn't exactly as labor leaders or workers had expected.

In the South Bend Lathe case for example, the USWA was not familiar with employee ownership and the buyout effort led by management. The resulting employee ownership plan included no worker representation on the Board of Directors, the pension plan was abandoned in exchange for the ESOP and the stock plan was structured for management control.

At the Herkimer Library Bureau the two unions again played passive roles. Worker owners initially felt elated at the dramatic success of their job saving campaign. Fifteen months later, however, presidents of the two Library Bureau unions reported dissatisfaction that nothing had changed in the way that the plant was run. The company now appears to be moving toward traditional ownership. Four members of management have recently purchased newly issued stock to acquire majority control of the company.

Taking the Lead:

In some cases the union has become involved in employee ownership efforts and led the efforts. At Hyatt Clark Industries and the Rath Packing Company, the UAW and UFCW negotiated legal structures that include significant union influence now and more in the future. At Rath, the union carefully structured the employee ownership plan to keep the local union in line with the national wage agreement once workers bought the company. Rath deferred, not cut, wages to buy stock. At both Hyatt and Rath, workers and the union have significant input at all levels of company decision-making.

It is critical to make information available to all interested workers throughout the buyout process. Employees want to be informed of events and decisions regarding worker ownership. Ideally, the following steps will ensure sufficient knowledge:

- Union meetings include discussion of employee ownership.
- The union newspaper provides timely, relevant information.
- The company newsletter includes information so that supervisors and management remain informed.
- Workers can form an in-plant committee of representatives to inform workers in their individual departments of events and decisions regarding worker ownership.
- Stewards and other union representatives disseminate information.

Differences in goals can exist between the international union and the local. Local union officers concentrate their energy on maintaining jobs, good benefits and working conditions. While international union officials share these objectives, they are also concerned with maintaining the standards won in the past in company-wide or industry-wide master agreements.

Employee ownership plans have sometimes involved some form of benefit reduction. In the more recent cases where employees have reduced benefits and bought stock, careful structuring of the agreement has permitted workers and the local union to remain in the master agreement. If stock and increased influence are exchanged for benefits, the local can remain symbolically in the master agreement.

In summary, if the union takes an active role and if it is informed of the options, unions can assure that employee ownership protects the interests of workers and their unions.

A Mobilized Community: In many cases, successful transfer to employee ownership has occurred where the firm being closed is the largest, if not the major employer in the area. Usually efforts aimed at preserving the local community are shared by government leaders, civic organizations, churches, the rest of the business community and local residents.

Broad local support can be generated by a full understanding of the total costs of the plant closing.

At the same time that the community tax base is reduced, needs of social services increase. **A more complete checklist of losses and costs to the community are listed as "Effects of the Closure" on page 66.**

Active involvement of local leaders and the larger community is often essential to gain valuable time to conduct feasibility studies, negotiate with owners, and secure financing for the purchase. In most successful cases extensive use of newspaper and television media calls attention to the threatened closure and its effect on the community. The outcome is often widespread concern and sympathy for the displaced workers and mobilized support to delay or prevent the closure or support a buyout.

In some cases, local business groups have mobilized support for the workers. Small businesses in a community have much to lose if a major firm closes in loss of purchasing power, decline of services and loss of population in the area if workers move.

Active political support is often critical to the success of the transfer of ownership. In the case of Rath, local political leaders pressured management to accept the workers' offer and assisted the group in securing federal monies. In the VAG buyout, the active involvement of Vermont's governor, the state legislature and area congressmen was essential in the effort. A state agency also financed a feasibility study and provided loan guarantees.

Churches and other social agencies have the potential for playing a major role in organizing the community. Grassroots support is critical, especially in worker/community ownership. In the case of VAG, the community pulled together and raised $1.5 million for the buyout. In Herkimer, workers and volunteers sold stock like raffle tickets and raised $1.8 million.

VIABLE FIRM

The most basic condition for success of an employee buyout is the economic soundness of the enterprise and its availability at an acceptable price. **A viable firm is one that has access to markets and raw materials, an efficient plant, qualified labor and experienced management, adequate capital, and current owners that are supportive of the buyout.** The reasons why these factors are so important is explained in the brief paragraphs below. **The way to find out whether these factors support a buyout decision is by way of a feasibility study.**

The feasibility study tells employees and others whether they should risk investing in an employee owned firm and what returns they can expect to earn. Not only should it guide the decision of current employees, it also will influence the decision of the community to support the buyout, investors whether to provide financing, and managers and entrepreneurs whether to work for a new firm. For these reasons, it is critical that the feasibility assessment be complete, professional, and credible.

Because an effort of this magnitude takes considerable time and money, the feasibility assessment has two parts; a preliminary study and an in-depth study. **The preliminary study indicates whether there are any reasons why an employee buyout definitely cannot succeed or why one clearly could succeed. It investigates whether the product is obsolete or in demand, the plant is obsolete or efficient, the present owners are amenable to a buyout, and the plant has the necessary organizational building blocks.**

Only if the preliminary feasibility study is positive, should employees proceed further. **The in-depth study investigates in detail the future demand for existing and new products, the viability of the plant with a small investment, whether financing can be obtained and what is the best business plan. Both the preliminary and final feasibility studies are described in later sections.**

Markets Exist: If the products that the employee owned firm intends to produce are obsolete or facing declining markets, the newly formed firm will offer no more job security than the existing firm. It may even exact an additional cost in the form of wages or severance pay given up to a losing venture. Thus, it is essential that the expected market be stable or growing for the firm's planned product line.

Plant Can Compete: For the employee owned firm to be able to take advantage of the market for its product, it must at least be able to produce at a cost that is less than its sales revenues. In addition, it must be able to provide products of equal or better price and quality as its competitors, and keep up with radical changes in industry production techniques and product offerings.

Smooth Transition Possible: There are a number of factors that determine whether a smooth transition is possible. The commitment of people is the most important since managerial expertise and leadership are critical for success. In nearly all successful cases one or more key local management representatives assisted the employee owned company. In several cases where this did not occur, efforts to recruit management leadership hindered the local effort to save jobs.

Employee efforts to secure key managers are often disappointing. A prospective chief executive officer (CEO) is unlikely to consider a leadership position in the new company until financing is located for the venture. On the other hand, individuals and organizations which could provide equity or loan capital are less inclined to commit money until they are persuaded that the new company has competent management. Until one or more key management positions are filled, it may be possible to substitute an outside financial expert to negotiate with lending agencies.

In addition to expertise, it is important that the employee owned firm can also depend upon not having to substantially alter its business structure. The transition will be smoother (and less risky), if the new firm (1) has all of the necessary business functions (marketing, sales distribution, finance, etc.), (2) was previously operated as a separate entity with its own profit and loss statements, and (3) did not previously receive many inputs from other plants or transfer outputs to other plants.

Current Owner is Cooperative: An initial hurdle facing employee buyouts is the relationship between the workers and the current owner. If interaction with the original company is positive, success is much more likely. If the current owners are unwilling to sell the company or plant, there is little that workers or the community can do to save the jobs. The active cooperation of the current owner in terms of early notification, a fair selling price and access to financial, technical and marketing information greatly contributes to success.

In the case of Esterville-Morrell, Youngstown Sheet and Tube, and Colonial Press, the lack of cooperation on the part of the former owner was a main reason for the failure of the buyout effort. However, in the case of Esterville-Morrell, workers and their union traded off benefits for a union/management controlled fund for new technology and worker input in decision-making. This negotiated agreement and the company improvements that it created kept Morrell open and workers employed.

Whether or not the previous owner cooperates is dependent upon several factors. In most of the cases outlined above the parent corporation did not readily see the employee purchase offer as a viable option. Top corporate management may not believe the employees have the skills to succeed or they may fear potential competition from a successful buyout if other units of the company produce the same product.

If management is cooperative, representatives of the workers should discuss very specifically with management the reasons for the closure and their advice on the best way to avoid closure if possible. The most important factors to touch on are the relative importance of market demand, age of the plant, lack of capital for modernization, regulations, taxes, inadequate profits, workforce problems, and transportation costs. Management should also be asked whether the production capacity is being shifted to another plant or plants, and whether this shift will add employment to these other locations, or merely use now idle capacity. **Additional information including sample questions concerning the cause of the closure are included under "Management Liaison," in Appendix V, page 65.**

If successful in developing a positive relationship with the current owner, the workers can gain substantial advantages in doing the feasibility study, negotiating a purchase price, and operating the new company.

Financial Backing is Available: The availability of private and public sources of capital is crucial to a successful worker buyout. Funding is necessary for the purchase of the facility, for inventory and equipment, for operating expenses and for the feasibility study prior to assembling the business plan. After determining financing needs, it is important to select an optimal financing plan. The financing plan will affect the feasibility of the venture. If interest costs are too high or there is too little stock, the new firm will not make it. The many financing choices and their implications are described in a later section.

TECHNICAL ASSISTANCE

Technical assistance from current owners and management, the government, and outside consultants improves the success of employee ownership attempts. Because management has a large amount of proprietary information on plant operations, information it shares will vastly improve the feasibility of the buyout attempt. Management may be able to make knowledgeable suggestions about everything from new products to financing sources.

Government's role in providing technical assistance is critical in most successful cases of worker ownership. The shape that such assistance takes varies from direct financial support to detailed technical planning. While its resources are limited, the State of California currently provides technical assistance to employee ownership projects to:

- Inform the community of the option and assess interest.
- Make information available in fact sheets.
- Promote and coordinate state, federal, and private agencies to assist in formation of the employee owned corporation.
- Provide technical assistance to form a Community Response Committee to undertake necessary tasks.
- Provide information on consultants for feasibility studies.
- Assist in locating funding sources.

The involvement of consultants and other outside expertise is also important in many cases of worker buyouts. In some cases, free professional assistance has been offered by lawyers, bankers, accountants, and religious and political leaders. University business and organizational behavior professors have also provided assistance to workers and communities. Paid consultants may be needed to perform feasibility studies and provide legal advice on how to structure the employee owned business. Where to find technical assistance and how to pay for it is described in a later section (Feasibility Study). **Sources can be found in Appendix A: Resources for Employee Ownership.**

VIABLE ORGANIZATIONAL STRUCTURE

While employees anticipating the formation of their employee owned firm to save their jobs may not be particularly concerned about rights to influence management and business operations, these issues are most important when the

employee owned firm is formed. In many cases, employees have discovered over time that their expectations about control and participation have not been met, and that they are powerless to change the results. Thus employees must pay attention to ownership structure and employee participation.

Effective Ownership Structure

There are many varieties of employee ownership. Both employers and workers can benefit from the use of some of these methods. Some workers and unions have been hurt and disappointed, however, by the results of employee ownership. Long-range planning is the KEY to making wise choices in this area.

The legal structure of the worker owned company lays the groundwork for the way the company is run, the way that decisions are made and, to a great extent, the nature of labor/management relations.

The key fact is that ownership and control do not always go together. In the past, worker ownership has usually involved a traditional stock ownership plan with voting rights based on shares of stock. If shares are allocated based on salary for example, management often accrues a majority of the stock. In two early community/employee owned firms, Vermont Asbestos Group and Mohawk Valley Community Corporation, workers owned a portion of the stock and the firms were run basically as they had been under traditional management.

At Vermont Asbestos Group, workers owned 78 percent of the stock, enough to constitute majority control. However, after several years, workers learned that ownership of a company does not mean influence over decisions. The 15 member VAG board of directors was made up of 7 workers, 7 salaried people and one outsider. Most decisions, however, were made by a 5-member executive committee made up of top management. Over time workers were confused over their role on the board, including the extent to which information could be shared with the rank and file. In addition, workers could sell their stock to anyone who offered to buy it. Thus, when the successful firm's stock went up in value, many workers, disillusioned, sold their $50 shares for $2,000 to a local businessman. Over time, an outside group obtained majority control of the once worker owned mine.

At the Herkimer Library Bureau, two-thirds of the stock was owned by the community while one-third was owned by the Library Bureau's workers and managers. After the start up, the company established an ESOP. Workers owned a majority of the shares but had little input in decision-making. In late 1980, the board of directors issued new stock to allow management to acquire half of all the voting stock, thus ensuring management a controlling interest in the firm.

In addition to these community/worker owned companies, several fully worker owned companies exist where the union was less active in structuring the ESOP. Occasionally, management initiates the employee purchase. South Bend Lathe, for example, was initiated by the plant manager. Management sought to maintain the traditional organization structure and workers do not receive effective control or voting rights on their stock until 3 years after the stock is allocated. With the South Bend stock plan, in 1980 workers owned 67 percent of the company but they can vote only 22 percent of the company stock. The other 45 percent ownership is held in employee stock which hasn't yet gained voting rights.

In contrast, more recently unions have negotiated for significant power in the new employee owned company. At the Rath Packing Company, the union led the effort to save jobs and structured the employee ownership plan to facilitate employee participation. The workers own 60 percent of the company stock and control the firm. Their stock is voted as a block through an Employee Stock Ownership Trust (ESOT). Five worker trustees are elected on the principal of one person/one vote. The power of the workers trust, which votes 60 percent of the stock in annual stockholders meetings, provides the basis for indirect worker control of the company. The trust influences stockholder meetings which in turn generates mandates for the board of directors, including selection of top management and making company policy. These managers then continue to direct the work force in day-to-day production.

This bottom up collective power allowed Rath worker-owners to hire management, including a new company president, monitor millions of dollars allocated for capital improvements, decide investment strategies, etc. The union also continues to represent workers in grievances and in negotiatons for the labor contract.

At Hyatt, the UAW Local 736 played a key role in negotiating the legal structure of the employee owned company. After negotiations the groups accepted the union proposal that stock be divided equally among all employees. Stock is held in a trust and can be sold only upon leaving the company.

A more complete checklist of key legal issues is included under "Legal Issues: Ownership Structure and Tax Options," in Appendix V, on page 71.

<u>Worker Participation</u>

A final critical issue to consider in the shift to worker ownership is the role of worker input into decisions in the new firm. Many employee owned companies are run exactly as they were prior to the employee buyout. In the late 1970s, however, we began to notice that in some of these companies workers expected to have more input in how things were done and how money was invested in the company.

In nearly every case, management prefers to maintain their traditional prerogatives. In contrast, worker owners come to expect greater rights to know about how the company is run and the right to be listened to by management. The labor management conflict that arises is often costly. Some of the early employee owned firms, which did not include worker participation, have recently had strikes. Care in structuring employee involvement can avoid many of these conflicts.

At South Bend Lathe, worker owners were initially enthusiastic. Yet, the new company president managed the new worker owned business exactly as before. In the first five years after the buyout, annual sales tripled and workers received numerous wage increases and bonuses. In 1977, 180 workers petitioned for 50/50 representation on the board of directors. In spite of economic achievements, workers went on strike in fall 1980, partially due to dissatisfaction over lack of worker input in company decisions. "We were promised a piece of the action," says John Deak, Sr., President of the local, "what we got was a misunderstanding." The company president notes that "labor problems have destroyed the kind of spirit we really should have in an employee owned firm."

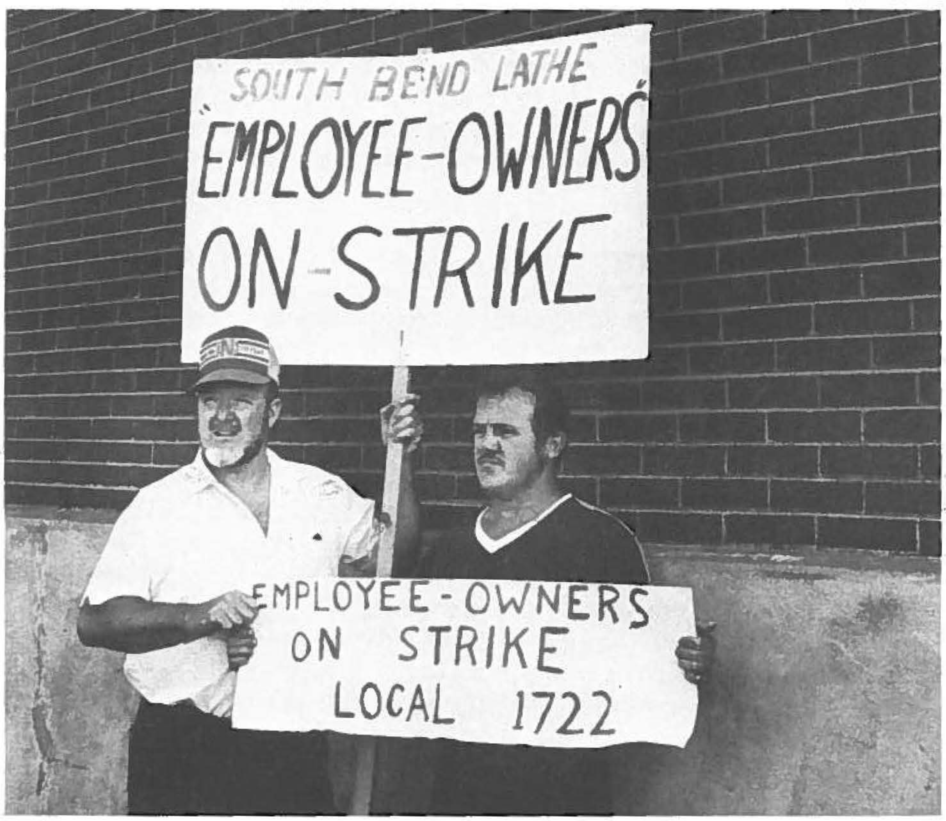
Workers carried signs saying "ESOPs Fables" and were thrown off of their company parking lot when a local judge ruled they couldn't picket there. Now the union is trying to negotiate full pass-through of voting rights to every employee equally. The company has recently offered to begin worker participation to improve worker input in decision-making.

At Okinite, 250 I.B.E.W. members in the North Brunswick Plant also went on strike in 1980. Newspapers reported that striking workers felt that "they (management) own the company, but we don't."

Likewise, at Jeannette Sheet Glass, the initial cooperative spirit waned in the first few months as workers saw management upgrading their offices while workers had a wage freeze. The two top managers hired from outside ran the plant like any other business. A committee was established for worker input, but it quickly became seen as ineffective. In 1981, 157 workers signed a petition taking the company to court over their right to be informed and to have access to the firm's books. Workers have been laid off, with the accompanying feelings of resentment and hostility.

Because of labor relations problems in these and other firms, in the most recent employee ownership plans union and management have created formal mechanisms for workers' input in decision-making. Both Hyatt Clark Industries and Rath Packing have labor management committees for cooperative problem-solving on all levels of the company.

Steps to establish labor management cooperative problem-solving can be found on page 75, in Appendix V.



Dissatisfaction over lack of input contributed to a strike by worker owners.

THE PRELIMINARY FEASIBILITY ASSESSMENT: SCREENING OUT INAPPROPRIATE CASES

Because the preliminary feasibility study's purpose is to be quick and inexpensive, it is only a means of identifying those cases where an employee buyout is very inappropriate (or appropriate). The preliminary feasibility study should take less than a month to complete and cost very little (usually much less than $2,000). If funding is not easily available, it can be prepared by qualified volunteers from community or government offices (such as the State Office of Economic Policy or Chambers of Commerce), on a pro bono basis by university business school faculty and students or consulting firms (such as the UCLA School of Business or Stanford University School of Business), or by public interest or nonprofit groups with low overhead (see Appendix I, Resources for Employee Ownership, page 54). Finally, the preliminary feasibility study should employ readily available sources of data that answer the specific questions described in the following sections:

(A) **Are the present owners amenable to an employee buyout?**

1. Is there language in your union agreement giving you first option to buy? (See Union Agreement) Yes _____ No _____

2. Is the standard language in union agreements giving management exclusive rights to manage and relieve employees removed from your agreement? (See Agreement) Yes _____ No _____

3. Has management been publicly willing to entertain an offer from employees or at least been neutral about such an offer? (Meet with management, read press clippings) Yes _____ No _____

4. Is management willing to contribute a nominal sum toward the feasibility study or to consider a decision to dedicate land, structures or equipment to the employees currently or in the future? (Meet with management) Yes _____ No _____

If the answer to the first question is yes, then lack of support by management should not be a problem. If it is no, then the answers to the other three questions are more critical. If the answers to questions 2 through 4 are also no, then management will probably be unwilling to negotiate a buyout with employees. As a result, a successful buyout is unlikely, and will be possible only if there is both significant media and public support, and a feasibility assessment indicating very clear benefits to employees and investors.

(B) **Is your firm organized in such a way that a smooth transition to employee ownership is feasible?**

1. Do you have an individual experienced manager, or group of experienced managers, who is willing to manage your employee owned firm? Yes _____ No _____

2. Do the skills of your work force meet the needs of your employee owned firm? Yes _____ No _____

3. Does your plant have on-site personnel, marketing, finance, and general administration functions? Yes _____ No _____

4. Is your plant operated as a profit center? (Is it required to document both its revenues and costs?) Yes _____ No _____

5. Does your plant produce its products without receiving inputs from other management owned plants or transferring outputs to other management owned plants for finishing? Yes _____ No _____

All of the above questions indicate whether a smooth transition is possible. The commitment of skilled top and middle managers is crucial. Nevertheless, if there are some potential managers, expert economic and legal advice by an outside consultant can substitute up to when a final decision is made to proceed. If the answer to one or more of questions 2 through 5 is no, then it is important that there be time to reorganize the firm before it closes and that there be committed management. If there are only a few months available (not enough time to reorganize), then an employee buyout is only advisable if plant and market factors are both very positive, improving the chances of continued interest once the plant closes.

(C) **Are the products produced at your plant facing declining, stable or growing markets?**

To answer this question in the preliminary feasibility analysis, you should rely on published analyses and industry experts. Prime sources of data on your industry available in libraries (such as public business libraries, university libraries, or major bank libraries) or from your company are as follows:

i. Standard & Poor's Industry Surveys
ii. Value Line Investment Survey
iii. Department of Commerce's U.S. Industrial Outlook (Annual)
iv. Moody's Industrial Manual for your corporation or other firms in your industry (Annual)
v. Walker's Manual of Western Corporations
vi. Dun & Bradstreet, Inc., Key Business Ratios
vii. 10K report of your corporation (look at statement of President)
viii. Market studies prepared for your corporation
ix. Trade journal articles on your industry located through the Business Periodical Guide and F&S Guide

Industry experts whose opinions you should seek out include the following:

i. The analyst for the appropriate industry from the Bureau of Industrial Economics, Department of Commerce, Washington, D.C.
ii. The trade association staff for your industry's trade association (See Trade and Professional Associations in California: A Directory, Center for California Public Affairs, Claremont, CA, 1979).
iii. Market analysts from market research firms or security analysts for your industry (ask reference librarian at a business library or get names from articles in trade journals).

iv. If possible, sales and production managers at your firm.

Using these data sources and others that become available, it should be possible to find sufficiently good answers for screening purposes to the following questions:

1. Do industry sources anticipate stable or growing demand for your industry's products? Yes _____ No _____

2. If there is a recession or slump in your industry, is it projected to end within 6 months to a year? Yes _____ No _____

3. If there are new or existing products taking market share away from (replacing) your product:

   a. Can your plant possibly produce the competing product? Yes _____ No _____

   b. Are there possible new markets or niches for your product? Yes _____ No _____

4. Are other producers of your product maintaining or increasing capacity or production levels? Yes _____ No _____

5. Are foreign firms or plants expected to maintain constant or declining share of U.S. sales over the next few years? Yes _____ No _____

6. If your product is sold to other industries (rather than consumers), do industry sources indicate strong demand for these industries' products? Yes _____ No _____

7. If there are obvious alternative uses for your plant, are the answers to the above questions for the alternative uses or products affirmative? Yes _____ No _____

8. According to industry analysts and plant managers, how does your product compare to that of other domestic and foreign producers:

   a. Average quality equal or better Yes _____ No _____
   b. Average prices equal or lower Yes _____ No _____
   c. Perception by customers equal or better Yes _____ No _____

It is important that most of the eight screening questions be answered "yes". It is imperative that at least the answers to 1, 2, 3 and 8 be positive for your product or for alternative products.

(D) Is it possible for your plant to be an efficient producer in your industry?

To answer the following questions, historical data will be needed on your plant. For part (1) of D in particular, it may be difficult to obtain the necessary data. Thus, if you cannot obtain data on your plant's current profitability, skip part (1) and go directly to part (2).

1. **How does the profitability of your plant or firm compare with other firms in your industry?**

   a. Data needs include one to three years of historical data for your facility on profits before taxes, sales revenue, net worth, and Robert Morse industry-wide financial data (for the SIC code that most closely corresponds to your firm*) on profit/sales and profit before taxes/tangible net worth.

   b. Procedures for performing the comparison are provided in worksheets 1 and 2.

   c. Criteria for judging the results are as follows: Has your average profit/sales ratio for the last three years been positive? (See line 4 of worksheet 1). Yes _____ No _____

      Is the average profit/sales ratio for your firm less than 50% of the industry average? (Your firm may not be competitive in your industry.) Yes _____ No _____

      Is the average profit before taxes/tangible net worth ratio for your firm less than the industry average for the lower quartile? (Your firm may not be competitive in your industry.) Yes _____ No _____

EXHIBIT 1

ROBERT MORRIS DATA

Current Data						Comparative Historical Data		
						6/78-1/77	6/77-1/78	6/78-1/79
0-25M	150M-1MM	1-10MM	10-50MM	ALL				
2	9	21	6	38		All 45	All 36	All 38
%	%	%	%	%		%	%	%
					INCOME DATA			
		100.0		100.0	Net Sales	100.0	100.0	100.0
		72.1		68.5	Cost of Sales	63.7	65.1	66.5
		27.9		33.5	Gross Profit	36.3	34.9	33.5
		22.7		28.3	Operating Expenses	29.3	28.8	28.3
		5.3		5.2	Operating Profit	7.0	6.2	5.2
		5.0		6.0	Other Expenses	9.0	5.0	5.0
		4.8		4.6	Profit Before Taxes	6.1	5.7	4.6
		35.2		35.2	% Profit Before Taxes/	38.7	37.2	35.2
		20.9		22.0	Tangible Net Worth	24.5	27.5	22.0
		9.0		9.0		10.9	9.9	9.0

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* The SIC code for your firm can be determined from descriptions in Standard Industrial Classification Manual, 1972, available at any business-oriented library. Examples of the two ratios from Robert Morris that are needed are indicated with arrows in Exhibit 1.

WORKSHEET 1

PROFIT BEFORE TAXES/SALES RATIO
YOUR FIRM
($s in 000's)

	Years 1 19__	2 19__	3 19__
(1) Total Sales Revenue	________	________	________
(2) Profit before Taxes	________	________	________
(3) Profit/Sales Ratio: Line (2) ÷ Line (1) multiplied by 100	_____	_____	_____
(4) Average of the three years for firm	_____		
(5) Industry Average Profit/Sales Ratio	_____	_____	_____
(6) Average of the three years for the industry	_____		
(7) 50% of Industry Average	_____		

EXPLANATION FOR WORKSHEET 1

Line (1) Total sales revenue from top line of the firm's income statement for last three years.

Line (2) Profit before taxes located on the firm's income statement for last three years.

Line (3) Line (2) divided by Line (1) multiplied by 100.

Line (4) Sum of Line (3) divided by 3.

Line (5) Industry Average Profit/Sales Ratio from Robert Morris data for same three years.

Line (6) Sum of Line (5) divided by 3.

Line (7) One half of Line (6).

WORKSHEET 2

PROFIT BEFORE TAXES/TANGIBLE NET WORTH RATIO
YOUR FIRM
($s in 000's)

	Years 1 19__	2 19__	3 19__
(1) Stockholder's Equity	________	________	________
(2) Intangible Assets	________	________	________
(3) Tangible Net Worth: Line (1) minus Line (2)	________	________	________
(4) Profit before taxes	________	________	________
(5) Profit before taxes/ tangible net worth: Line (4) ÷ Line (3) x 100.	_____	_____	_____
(6) Average of three years for firm	_____		
(7) Industry Average Ratio (lower quartile)	_____	_____	_____
(8) Average of three years for the industry	_____		

EXPLANATION FOR WORKSHEET 2

Line (1) Stockholder's equity from the firm's balance sheet for last three years; include common stock plus paid-in surplus and retained earnings and subtract the value of any treasury stock.

Line (2) Sum of all intangible assets shown on balance sheet for last three years such as "goodwill" and "cost in excess of net assets of acquired companies."

Line (3) Line (1) minus Line (2).

Line (4) Profit before taxes located on the firm's income statement for last three years.

Line (5) Line (4) divided by Line (3) multiplied by 100.

Line (6) Sum of Line (5) divided by 3.

Line (7) Industry Profit before taxes/tangible net worth ratio for the lower quartile of firms from Robert Morris data for same three years. This figure should be taken from the bottom row of figures because this row represents the lower quartile.

Line (8) Sum of Line (7) divided by 3.

If the answers to both of the tests of profitability indicate that your firm is not competitive in your industry and your profit to sales ratio is negative, then an employee buyout is unlikely to be successful unless there are glaring reasons to expect a significant change in profitability under new management. Examples of such good reasons include documentation that management has transferred production of profitable products to other plants, there is excessive corporate overhead, waste of materials, or salaries compared to past years of operation or other plants, or that there are obvious missed market opportunities. These reasons may not be sufficient, if the plant is not in good shape to take advantage of these opportunities.

2. **Has your plant been maintained and can major capital expenditures be avoided?**

   a. Data needs include plant maintenance records, plant capital spending budget, industry data on technologies employed and new facilities built, and data on profit after tax and depreciation expenses. If these data are not available, use your best judgment.

   b. Criteria for evaluating this data are as follows:

      i. If your plant and equipment are older than the average for the industry, have they been maintained.
      Yes _____ No _____

      ii. Have all major capital expenditures that are necessary to maintain the facility, or meet government regulations (ex. pollution control) been made? Yes _____ No _____

      iii. Does your plant have processes and technologies at least as current as those used by the majority of your industry? (based upon your market research.) Yes _____ No _____

      iv.* If your plant has not been maintained or has not met government regulations, would the cost be reasonable to make necessary expenditures? A benchmark is whether the cost crudely estimated to get your facility in good condition would be less than six times your plant's average cash flow (profit after tax plus depreciation expenses) for the last three years? Yes _____ No _____

      vi.* If your plant's processes and technologies are not current (based upon your market research), would the cost be within reason to make necessary expenditures? A benchmark is whether the cost crudely estimated to make required maintenance on your facility and obtain the new technologies

* Skip this question if data on the profitability of your plant is not available. If this data is available, add together profit plus depreciation expense for last three years and divide by three. Then multiply the result by six. The capital cost of new equipment should be smaller than this result.

would be less than six times your plant's average cash flow (profit after tax plus depreciation expenses) for the last three years? Yes _____ No _____

If the answers to the first three questions above are yes, then your plant is in good condition and up to date. If the answers are no, then you need to consider how costly it will be to bring it up to date. A benchmark is provided in the fourth and fifth questions. If the answers to all five questions are no, then a successful buyout is unlikely because of poor plant maintenance combined with high capital costs. A minimal requirement is that either the plant is adequately maintained or that costs of achieving adequate maintenance are not exorbitant.

(E) Summary of the results of the preliminary feasibility study

At the completion of the preliminary feasibility study, the following questions should have been posed and answered:

- **Is there enough time before the closure? (See Factors for Success)** Yes _____ No _____
- **Are the present owners amenable to an employee buyout? (See (A))** Yes _____ No _____
- **Is your firm organized in such a way that a smooth transition to employee ownership is feasible? (See (B))** Yes _____ No _____
- **Are the products produced at your plant facing stable or growing markets? (See (C))** Yes _____ No _____
- **Is it possible for your plant to be an efficient producer in your industry? (See (D))** Yes _____ No _____

In an optimal buyout situation all of the answers will be yes. This will rarely be the case. In most cases, the most important questions are the last three. While there will often be special circumstances beyond the scope of this manual, in general, affirmative responses to the last three questions and, in particular, those about efficiency of production and market for the product, are crucial.

THE FEASIBILITY STUDY: WHO TO DO IT, HOW TO PAY FOR IT, AND WHAT BELONGS IN IT

If the preliminary feasibility study indicates that an employee buyout is potentially feasible, a full-scale feasibility study is needed. The purpose of the feasibility study is to provide a comprehensive assessment of risks and opportunities for the employee owned firm.

Several experts are needed to perform the study and guide the necessary followup:

- o Financial consultants to do the study;
- o ESOP or co-op experts to structure the buyout; and
- o Lawyers to negotiate the purchase of facilities.

In addition, in some cases a real estate appraiser will also be needed. The costs of obtaining these experts and the way in which their services will be used is described in the following paragraphs.

Costs That Will be Incurred and How to Finance Them

The cost of the feasibility study will depend upon the specific case, but some estimated costs as of 1982 are provided in Table 5. This table assumes no free services or below market cost services.

Table 5
Cost of Feasibility Study

For cost analysis using available data and review of public market research	$ 20,000
If market research is required	+20,000
	$ 40,000
If must generate new cost data because of anticipated changes in products and markets	$+20,000
	$ 60,000
If must appraise assets	$+15,000
	$ 75,000
If need lawyer and ESOP expert	$+40,000
	$115,000

The feasibility study and follow-up will cost at least $20,000 and may cost more than $100,000.

Costs can be minimized by seeking out consultants with low overhead and firms willing to do pro bono work. It can also be done by using consultants who have a good reputation, but do not have a well known reputation. These consultants can be backed up with an oversight committee. This committee should include local bank officials, ESOP/co-op experts, a law firm, city officials, union representatives and management consultants.

There are a number of sources of financing for the feasibility study. The main ones are described below.

(1) Raise money from union members--it is a good idea to request at least a small contribution as a sign of commitment--and from existing owners.
(2) Obtain grants from federal agencies such as the Economic Development Administration--while this approach is time-consuming, it worked for the U.S. Steel Youngstown employees who received a grant to hire a consultant.
(3) Obtain technical assistance grants from State agencies--the State of California approved a grant to help General Electric workers in Ontario to perform a feasibility study.
(4) Local Economic Development Department grants.
(5) Local benefactors, perhaps located through the mayor's office.
(6) Foundations and churches.
(7) Making use of pro bono work by business schools, firms and universities.

How to Find and Choose the Consultants

The most likely sources of consultant support for the feasibility study are management consulting firms, other financial consulting firms, Industrial Cooperative Association and other nonprofit groups specializing in worker ownership, and university business schools (for both faculty and students).

Finding appropriate people can be difficult, but there are several good starting points. You can ask (1) state economic research offices (such as the Office of Economic Policy) that have contact with economists and business analysts or state departments that service your industry (Department of Forestry, Energy Commission, etc.), (2) Chambers of Commerce or Industry Trade Associations, whose members may have used business consultants, (3) university MBA programs where you can ask the dean of students whether students undertake business consulting projects and (4) department heads of university marketing, finance, and business policy departments who may know the faculty who do this kind of work. In an attachment there is a list of Resources for Employee Ownership that offers advice on sources of assistance (there is also a list of guide books, etc.).

Once you have found one or more likely individuals or groups, there are several questions that you should ask them. These are listed in Table 6.

Table 6
What to Look for in Potential Consultants

1. Have they done other cost analyses of plants?
2. Have they done any market studies?
3. Have they done financial modeling or prepared business plans?
4. Have they had other business clients?
5. Have they done feasibility studies for plant buyouts or divestitures?
6. Do they have backgrounds with extensive business/finance experience?

7. What are the names of some of their clients, and can you call them to get their opinion of the individuals?
8. Is overhead less than 100% of their hourly cost?
9. Can they get the study done within a few months (depending on your time pressures)?
10. Are they willing to give caveated opinions about issues for which all the data they would like is not available?

The Feasibility Study: Content and Interpretation

The purpose of the following discussion is not to describe how to do the feasibility study. The specific steps vary significantly from case to case, and the employees certainly don't need to be able to perform the analyses. Nevertheless, they do need to be concerned about whether the feasibility study deals with the relevant issues, and they need to know how to interpret the results. **There are two basic parts to the feasibility study:**

(A) **Market Factors--demand for the product.**
(B) **Plant Factors--viability of the plant with a small investment.**

While a related area is financing, whether financing is obtainable will depend on the market and plant factors. Thus, financing is discussed separately in a final section.

Relevant Issues to Analyze in Feasibility Study

The following sections describe the relevant points that the consultant should investigate and the results that employees should seek. It may be desirable to have a contract with a consultant that requires the following analyses:

(A) Market Factors

1. Future Market for Each Product Produced

   - short-term and long-term demand outlook
   - new uses for your products
   - new substitutes for your products
   - new potentially profitable product lines
   - new competition from abroad
   - if your product is an input for another product, short-term and long-term outlook for industry using your product
   - your market share by product line
   - shifts in your market share
   - if market changing, niches for your product

   Results sought:

   Whether you can expect continued demand for your products and, if so, approximately how many units can you expect to sell.

2. Concentration/Competition in the Industry

   - type of market (local, regional or national)
   - number or changes in number (new plants, plant closures) of firms in market

- names of dominant producers and estimates of their market shares
- changes in imports
- new production technologies; whether your plant has them and their importance
- integration of your facility relative to competitors
- distance from markets relative to competitors

Results sought:

Whether your firm has any unique advantages or disadvantages relative to competitors.

3. Feasibility of Competition By a New Entity

(i) Basis of competition for customers in your industry

- importance of brand name
- number of brands
- homogeneity of product
- effectiveness of price cutting
- whether existing firm is major brand
- how existing firm has competed

Results sought:

Whether the employee owned firm will be able to compete for customers.

(ii) Normal Industry Distribution Channels

- do most firms in industry use factory direct sales, distributors or manufacturers' representatives?
- channels existing management has used
- what distribution facilities (ex: warehouses) will the employee owned firm need, and are they available?
- can the firm keep its existing distribution channels and contacts? If not, are there channels it could easily adopt?
- will the firm need to obtain a large new sales force?
- are customers willing to purchase goods from the new employee owned firm?
- are any large customers willing to provide letters of intent to purchase from the new firm?

Results sought:

Whether there is a means of distribution available to the employee owned firm that will not require a complex, new network.

(iii) Sources of Inputs at Competitive Prices

- current suppliers of inputs (raw materials, etc.)
- potential new sources of inputs
- do current suppliers serve other facilities owned by your corporation?

- will you be able to keep suppliers?
- will the employee owned firm purchase a sufficient amount of inputs to command competitive prices?
- are there any very large suppliers of inputs?
- are any large suppliers willing to provide letters of intent to sell to the new facility?

Results sought:

Whether the employee owned facility can expect to have reliable sources of supply at a competitive price.

(B) **Plant Factors**

1. Physical Condition of Plant and Equipment

- historic maintenance schedule and changes in maintenance
- historic reinvestment plan and changes in plan
- average age of major capital equipment and remaining useful life of equipment
- age of facility relative to average age for other plants owned by parent firm and by other firms
- need for major capital expenditures for maintenance, modernization, and/or regulation compliance
- estimated value of plant and equipment to be purchased*

Results sought:

Whether the facility has been maintained enough to allow continued productive use. Whether large capital expenditures can be avoided, at least in the first three to five years. Which of the facilities for sale are needed by the employee owned firm, and their maximum value to the new firm.

2. Organizational Structure: Leadership, Functions and Facilities

- is facility profit center or cost center?
- functions that would be included in purchase of facility, including personnel, marketing, sales, finance and general management
- personnel needed to fill gaps in functions
- are the facilities at the plant complete or would additional facilities be required, such as warehouses?
- ability to keep top and middle management on board or attract new experienced management
- does the existing work force have the necessary skills to operate the employee owned facility? is it willing to do so?
- products or services transferred from other plants
- products transferred to other plants

* A well-qualified appraiser of assets may be needed for this analysis. The appraisal will cover land, buildings, inventory, and equipment that will be useful for the new company. The business is worth the market value of its assets that are necessary to conduct business plus a premium if the business is especially profitable or minus a discount if it is unprofitable.

Results sought:

Whether the employee owned firm can have a smooth transition. This is determined by whether it can function as an independent facility without needing to be reorganized; whether it can be separated from current ownership without losing key suppliers or markets, and whether it can depend on having a committed management to lead it.

3. Historical Viability of the Plant

a. Economics of the Plant/Company

(i) Cost Structure for last three to five years: for each product line, including costs of materials, labor, energy, maintenance, allocated overhead and number of units of output.

- whether any unit costs are assessed at transfer prices (if so, revalue them to market prices)
- changes over time in the shares of costs and reasons
- changes over time in the usage of any input and reasons
- historical capacity utilization and efficient utilization levels

(ii) Operating Margins, computed using historical prices and costs

- trend in prices and reasons
- product lines with largest margins
- adjustments to mix that would increase plant margins

(iii) Break-Even Volume

- minimum volume of output at which revenues equal costs
- volume of output that maximized profit margin
- implications of optimal output for necessary changes in current output and employment for employee owned firm
- feasibility of being able to sell optimal output given market projections about size of total market

(iv) Profitability, computed based upon earnings data for facility for last five years or by subtracting from operating margins, unallocated fixed costs, estimated corporate charges, current interest costs and depreciation expenses

- trends in profitability
- how changes in mix identified above would change profits

(v) Cash Flow, for the last five years using the data above on profits (after tax computations), adding back depreciation expenses, and subtracting out changes in working capital, debt repayment and capital expenditures

- whether cash flow provided by operations has been sufficient to support necessary expenditures (compare profit plus depreciation to capital expenditures and debt repayment)

- if there are costs hanging over the plant for deferred maintenance, deferred replacement or regulatory compliance, has plant cash flow been sufficient to finance them? If not, how much outside capital would be needed to finance them?
- if the prospective buyout has been an independent business, additions to debt or equity capital in the last five years
- whether any of the facility's assets are secured by debt

Results sought:

Whether the facility has historically shown economic viability, including whether it has been able to control its costs and maintain profit margins; whether it has operated at optimal levels of output and with an optimal mix of its products; whether the new worker owned firm could expect a market for the volume of output at which it breaks even and for the volume of output at which it maximizes profits; whether it has been able to finance through internal cash flow its own working capital and at least some of its other capital needs; and whether it has been able to raise any outside capital in the past. For all of the above, what were the reasons why the firm did or did not achieve these profit, output, and financing aims.

b. Plant Strengths and Weaknesses (based upon the previous market and cost analyses)

- reputation of the facility, including whether it has long-term suppliers and customers and their satisfaction with the facility
- willingness of suppliers and customers to deal with the new firm
- quality or efficiency as a producer relative to other producers
- low or high cost producer in its industry for each product
- unique product offerings
- other strengths and weaknesses

Results sought:

Whether the facility has the good will of its suppliers and customers; whether these suppliers and customers will deal with the new firm; and whether its competitiveness with other facilities is enhanced or reduced due to specific strengths or weaknesses.

c. Feasibility of Improving Operating Margins, Profitability, and Cash Flow

(i) Ability to Control Costs

- cost reductions that could be made and their effect on profit margins; in particular, feasibility of reducing overhead, improving inventory control, reducing spoilage, and waste, reducing absenteeism, finding cheaper suppliers, and willingness of employees to trade off ownership for wage reductions (level of deferrals they are willing to consider)

(ii) Ability to Change Mix and Level of Output

- change in mix that would raise overall profits
- changes in output that are within the limits of the market that would raise overall profits

(iii) Ability to Raise Prices

Based upon market study, is it possible to raise prices and roughly by how much?

(iv) Ability to Introduce New Products

- what are compatible new products (see market study)
- operating margins on these products versus existing products

Results sought:

Whether profits can be increased by moderate cost reductions, changes in mix, changes in level of output, the introduction of new products, or price increases.

d. How Economics Would Change for the Employee Owned Facility

(i) Analyze the effect on profitability and cash flow of:

- the feasible changes in costs, prices, product mix and products investigated above
- different levels of capacity utilization
- required replacement of management staff and/or corporate functions
- training costs for new employees
- lower wages
- initiating new sources of supply and/or customers
- making deferred replacement, maintenance, and modernization expenditures

(ii) Compute estimate of future operating margins, profits and streams of cash flows for three years, taking into account the effects of the changes in (i) immediately above.

(iii) Compute working capital needs. If there is no good basis to estimate working capital needs, an approximation would be total operating expenses for four months (including rent, inventory, wages, leasehold improvements and known interest costs) plus reserve to carry accounts receivable plus petty cash.

(iv) Estimate costs of purchasing necessary facilities from existing owners or others (see Plant Factors.) Also estimate financing costs based upon your expectations as to sources of financing and potential cost (see Financing Section).

(v) Compare the estimated cash flows to the sum of the costs estimated in (iii) and (iv) using net present value analysis.* This step will need to be repeated once financing costs are more exactly estimated.

Results sought:

Whether the employee owned firm can achieve a rate of return high enough to maintain an efficient facility, pay back its lenders, and repay the employees for their investment.

* Net present value analysis is a technique that allows you to compare income you receive in the future to cash you pay out now to buy the plant. It takes into account the fact that both inflation and the ability to invest money now and earn a return rather than spending it reduce the value of income received in the future.

Evaluating the Results of the Feasibility Study

Once the results of the feasibility study are obtained, the employees must decide whether to proceed with the proposed employee buyout. In those cases where the results concerning market factors, plant factors, and potential improvements in these factors are overwhelmingly negative or positive, the decision may be easy. Because this will generally not be the case, it will be necessary to weigh the results carefully, considering the difficulties posed by each problem. The following rules will be of some help in this task. Other sources of advice include the consultant that prepared the feasibility study and potential investors in the firm.

The questions in Table 7 below should be answered in the course of the feasibility study. For an employee buyout to be advisable, either:

(1) **The answers to all of the "market" and "plant" questions in Table 7 should be affirmative; or**

(2) **The answers to all of the "market" questions in Table 7 should be affirmative and any answers to "plant" questions that are negative should be cancelled by positive options under "potential improvements."**

Of course, there will be situations in which a decision is made to proceed when these preconditions are not met. The employees in these cases must present to investors and themselves convincing reasons why the new firm will succeed. The document used to convince investors to participate in the buyout is the business plan. This document, as well as financing options, is discussed in the last section on Financing a Worker Buyout.

Table 7
Relevant Questions in Buyout Decision

Market Factors

1. Can you expect continued demand for your products and, if so, approximately how many units can you expect to sell? — **Yes ___ No ___ Number ______**

2. Is it likely that your firm will be able to compete for customers? — **Yes ___ No ___**

3. Is there a means of distribution available to your firm that can be put into place in time to ensure uninterrupted distribution? — **Yes ___ No ___**

4. Can your firm expect to have reliable sources of supply at a competitive price? — **Yes ___ No ___**

Plant Factors

1. Has the facility been maintained enough to allow continued productive use? Can large capital expenditures be avoided in the next few years? — **Yes ___ No ___**

2. Does your firm have or can it obtain necessary staff and facilities to function independently as soon as a transition is made to a worker owned firm? Yes ___ No ___

3. Can your firm retain current key suppliers and markets? Yes ___ No ___

4. Does your firm have, and can it continue to keep, the good will of its suppliers and customers? Yes ___ No ___

5. Does your firm have a committed management to lead it? Yes ___ No ___

6. Has your firm historically earned a profit? If not, was it due to causes that can be reversed? Yes ___ No ___

7. Would your firm break even given expected sales volume from the "Market Factors" section, question 1? Yes ___ No ___

8. Can your firm expect to be able to finance its own working capital and some part of its other capital needs after one year of operation? Yes ___ No ___

Potential Improvements

1. If your firm historically has not earned a profit, can profits be improved through moderate cost reductions or price increases? Yes ___ No ___

2. Can profits be improved through changing levels of output, mix of products, or introduction of new products? Yes ___ No ___

3. Can profits be improved through taking better advantage of unique characteristics of your firm? Yes ___ No ___

4. Can your firm achieve a rate of return sufficient to maintain an efficient facility, repay its lenders, and repay employees and investors for their investment? Yes ___ No ___

FINANCING A WORKER BUYOUT

If the results of the feasibility study are positive and the employees want to proceed with a worker buyout, in most cases external financing will be required. The document that will be used to determine which financing alternatives to pursue and to convince potential investors of the credibility of the venture is the business plan. The business plan is described below, followed by discussion of financing worker buyouts.

THE BUSINESS PLAN

The formal business plan is only needed if the decision is made to proceed with the employee buyout. The purpose of the business plan is to describe how the employee owned business will be set up and what are its prospects. **The plan is a guide for decisions following the buyout: both your decisions about operations and the decisions of investors about your likelihood of succeeding.**

Most of the sections of a business plan can be taken directly from the feasibility study. Thus, the most important point in this section is that the results of the feasibility study must be presented clearly and forcefully. An outline for the business plan is described in Table 8. The plan can be pulled together by whoever prepares the feasibility study.

Table 8
Contents of a Business Plan

I. Summary of Key Facts About the New Business

   A. Products

   B. Markets

   C. Projected profitability

   D. Key people

II. Narrative Portion

   A. Description of the new business, including its location, product lines and products, and facilities.

   B. Demand for the new business' products, expected markets, and sales strategy.

   C. Competition in the above markets, and strengths and weaknesses of the business relative to the competition.

   D. Management structure, experience of key managers, and skills of personnel.

   E. Cooperative ownership structure.

   F. Financing needs and planned uses of loan proceeds.

III. Analytic Portion

A. Projected statements of income, balance sheets, and funds flow (monthly for year one, quarterly for years two and three).

B. Explanation of underlying assumptions for these statements, including pricing, volume, wage costs, expected costs of supplies, fixed costs, and capital expenditures.

C. Description of these statements, including expected break even point, profitability, generation of cash flow for working capital, and anticipated rate of return on investment.

D. Anticipated problems in implementing the business' strategy, contingency plans, and resulting changes in financing projections.

FINANCING WORKER BUYOUTS

It is extremely difficult to obtain capital to purchase and operate a plant under worker ownership when the alternative is closure or drastically reduced operations. The process of convincing lenders is quite similar to that of convincing workers that operation of the plant can be feasible and profitable, except that lenders are much more skeptical and wary of workers running businesses. This section is intended to provide some guide to thinking about the financial aspects of the purchase. Additional references are listed in Appendix I which will provide further details on terms of private finance.

The financial structure of a corporation largely determines who controls the business. **Thus a first rule of financing worker buyouts is that the employees should put as little of their own money into the purchase and operation as possible. However, they should always retain majority control of the voting stock.** At a minimum, this requires that over 50% of the stock ownership is held by employees or a trust controlled by employees. If less than half is owned by employees, it is quite likely that outside owners will at some point disagree over the proper management of the business - seeking layoffs during recessions, asking for dividends rather than reinvestment, or other policies which may not be in the interest of worker/owners. Consequently, the first type of capital that buyout organizers should seek is debt finance or loans.

Loans are usually required for both short-term needs and long-term needs. Long-term loans are used to pay for the purchase of long-lived assets such as land, structures, and equipment, while short-term loans pay for financing purchase of materials, salaries, advertising, research and development and a variety of other current expenses. Except when long-term interest rates are very high and expected to fall sharply, it is advantageous to borrow money for as long as possible. This allows the business to plan its operations without worrying about refinancing a short-term loan and can lower the monthly or quarterly payments by spreading out the repayment of principal over longer time periods. Because of the desirability of long-term loans, they will be discussed before short-term finance.

Long-Term Loans

Except for the largest corporations, lenders will require collateral, or something of value, which can be repossessed by the lender in the case of default.

Because they have continuing value, land and structures are usually used as collateral for the loans used to purchase or construct them. Less frequently, but still quite normally, equipment, unless very specialized, can also be used for collateral. Typically, a lender such as a commercial bank, savings and loan association, or commercial finance company, will lend about 80% of the market value of these types of assets. This will require someone else to put up the remainder. No lender will make a loan, even if fully collateralized, if they think there is a major chance of default. The process of foreclosure and collection is sufficiently unpleasant to deter nearly all lenders.

A major alternative to financing through long-term debt is a sales/leaseback agreement. Under such agreements, the purchasers in effect simultaneously buy the structure and equipment and sell it to an outside group of investors who agree to lease it to the new company. The lease payments are sufficient to cover the cost of purchasing the assets (i.e. to pay off a loan used to buy them) but are usually smaller because the outside investors are able to take advantage of the investment tax credits and depreciation deductions that a new worker owned company in its initial stages probably could not utilize. There are three general categories of long-term lenders that a worker owned corporation should seriously consider: public agencies, the parent company, and commercial lenders.

Public agencies have been active in most worker buyouts because there is usually a substantial degree of risk involved and public lending agencies are somewhat susceptible to political pressure. The Small Business Administration, the Economic Development Administration, the Farmers Home Administration, and the Department of Housing and Urban Development are federal agencies with programs which can make loans to worker buyouts. All have previously played a role in financing worker ownership in plant closing situations. For example, the Department of Housing and Urban Development was instrumental in financing the Rath Meat Packing buyout, while the Economic Development Administration financed the South Bend Lathe buyout.

All of the relevant programs have faced budget cuts in recent years, and competition for their loans is quite fierce. Such public loans are usually at much more favorable terms than private loans, with both lower interest rates and longer repayment periods. A major problem with public lending agencies is that they normally require a great deal of time to process applications and make decisions on a buyout, which almost by definition requires fairly rapid action. In addition to these large federal programs, there has been a rapid proliferation of state and local loan programs (many of them funded by federal grants) which in some cases can be used to finance worker buyouts.

Some worker buyouts have been financed with the type of "seller financing" now common in housing finance, where the seller of a facility agrees to lend a portion of the purchase price to a borrower who either could not obtain normal loans or is unwilling to pay very high interest rates. There are two reasons why a large company considering closing a plant would consider providing capital for a worker buyout. First, as in the case of General Motors - Hyatt Clark, the company may want to maintain a business relationship with the new firm for purchase of the materials it has produced itself in the past, but at a lower cost. Second, it may be willing to finance the buyout to avoid harmful publicity about the closure. This non-traditional financing may also be available in part from suppliers or customers of the plant who will be harmed if it goes out of existence.

With this kind of "seller financing," the repayment period is usually less than desired - perhaps three to six years - but sufficient to allow the new firm to become established and present traditional lenders with a track record which justifies a loan. A less direct way in which the parent corporation might finance a buyout would be to guarantee a private loan or a tax-exempt industrial revenue bond.

Few worker buyouts have been accomplished without the aid of either public sector agencies or the divesting parent corporation. This is simply because the buyouts have been seen as far riskier than the traditional investments of private lenders. For example, the normal loss rate for commercial banks is no more than 1%, while most worker buyouts have certainly appeared to have a chance of failure much greater. Compounding the true risk is the simple fact that most private lenders are unfamiliar with worker ownership and unclear how to finance it. The major lenders for long-term loans are usually life insurance companies (which have been somewhat active in social investments in the past and one major insurance company did extend a loan to Hyatt Clark), commercial banks, savings and loan associations, and commercial finance companies. The terms available will never be as advantageous as those available from public lenders or sellers. Early contact should be made with local financial institutions, and it may be helpful to have local businesses dependent on the plant for sales or inputs contact their own banks for assistance.

Short-Term Loans

Short-term loans are usually used for what is called working capital - the money used to pay for the current activities of the company - salaries, inventory, materials for production, office supplies, and marketing costs. For companies in seasonal businesses, the level of working capital varies dramatically over the course of the year. Some activities, such as inventory, materials, and office supplies, are relatively easy to finance because they represent collateral. Many lenders, from commercial banks to finance companies, to suppliers themselves, will make loans based on these tangible goods. However, working capital needs for other purposes, particularly salaries and marketing costs, are far more difficult to finance, and usually must be handled out of current receipts and retained earnings for newer companies unable to obtain loans based on their past performance.

In recent years, some companies have used limited partnerships to finance both research and development costs and advertising campaigns. The limited partnership allows a company to raise money from outside investors who are interested in obtaining tax writeoffs. The typical arrangement calls for these limited partners to pay for some specified activity - like research or advertising - in return for deducting the costs on their tax returns and a percentage of future sales which result from the research or marketing. For a worker buyout, such deals may be an attractive way to involve local investors in the activities of the new company in a way which provides them with sufficient tax advantages to generate high profits but not give up control of the company.

Equity and Ownership

It is highly unlikely that the methods of obtaining loans discussed above will raise all of the capital required to purchase and operate a plant. Most public and private lenders will require some contribution on the part of the owners of a new company. Alternatively, they may demand collateral beyond the value of their loans, leaving the firm short of assets to finance working capital. If the new firm wishes to maintain majority ownership in the hands of employees, then the last source of capital which should be tapped is the employees themselves.

This is consistent with the way most new businesses are started. Very few new firms start with outside stock ownership, but instead rely on the savings of the founder. If the plant to be purchased is actually viable, it should be possible to convince at least some outside lenders, whether public or private, that their loans will be safe. It is usually impossible to finance an entire buyout solely on the financial resources of the workers.

If the workers put in their own capital, it may come from a variety of sources. In some cases, the divesting firm may make severance payments to workers which could be used as part of the purchase price. In others, workers may have savings, or be able to borrow against life insurance policies or the equity in their homes. Finally, in some cases, it has been suggested that workers use their vested pension fund assets to purchase a plant. In making these personal investment decisions, it should be kept in mind that in the case of failure, stock investments are the last to receive any payment, and workers should only invest money they are able to entirely lose. This argues strenuously against using pension fund assets in plant closing situations.

Understanding Your Balance Sheet

Table 9 depicts the balance sheet of an average manufacturing firm. This balance sheet can be used to clarify the preceeding descriptions of short-term and long-term financing needs and sources.

Balance sheets depict a firm's sources and uses of funds at a given moment in time. Sources of funds include debt, stock, and retained earnings. Uses of funds include purchases of assets and repayment of debt. These sources and uses of funds appear on the balance sheet as assets, liabilities, or stockholder equity. The dollar value of total assets equals the value of liabilities, plus stockholder equity. In this case, both values are $10,000,000.

Assets include very liquid items like cash and very illiquid items like property. Short-term and long-term loans plus other obligations of the firm make up its liabilities. Short-term loans are often used to fund relatively liquid (or current) assets such as inventories and accounts receivable. Long-term loans or stock are used whenever possible to fund illiquid (or long term) assets such as equipment, buildings, and land. Stockholder's or owner's equity consists of stock and retained earnings. These sources of funds are kept separate from liabilities because there are no contractual obligations to make payments on specific dates.

The average manufacturing firm in Table 9 has current assets of $4,454,570. The company must hold current assets to obtain orders and satisfy customers. Up to a point, more cash, receivables, and inventories will save money or produce enough additional revenues to be worthwhile. Beyond this point, further investment in current assets is a sign of poor management. The manufacturing firm in Table 9 has 45 percent of its assets in current assets.

Whether this is the appropriate share is usually determined by comparing the firm to other firms in the same industry. If the industry average is 50 percent, then the firm in Table 9 would be in the right range.

The manufacturing firm in Table 9 has current liabilities of $2,677,249. These current liabilities include short-term loans and trade credit that probably has financed materials, payroll, rent, and other short-term operating needs. While the best guarantee of repayment on such short-term loans is net operating profits, current assets also provide some indication of ability to repay loans by way of a comparison of current assets to current liabilities.

Net working capital is equal to current assets less current liabilities. A net working capital cushion provides a margin of safety for times when operating profits may be lower than average. At these times, current assets can be reduced to meet debt obligations without impairing the firm's ability to obtain and fill orders (i.e. it can continue to carry sufficient inventories and give short term credit to customers). Thus, whether the firm's net working capital of $1,777,321 appears to be adequate will influence its ability to obtain short-term loans. The firm in Table 9 has 1.66 times as much current assets as current liabilities. Again, whether this is adequate will be determined based upon the average for other firms in the industry as well as the strength of earnings.

A key measure of the risk of providing this average firm with a long-term loan is its debt to equity ratio, or long-term debt divided by stockholder equity. The firm in Table 9 has a debt to equity ratio of .34. This ratio gives some indication of a danger to the company's solvency of debt retirement and interest requirements. If it is too high, the firm may not be able to meet all of its obligations. If it is too low, the firm is not taking advantage of the leverage provided by debt. (Debt allows the firm to fund assets without giving up ownership or reducing the value of existing stock.) Of course, a great many other factors also enter into a determination of risk associated with a given equity structure, including earnings, asset reserves, and debt maturity structure.

SUMMARY POINTS OF THE FINANCING SECTION

(1) **obtain as much external capital as is possible in the form of loans;**

(2) **avoid any financial package which places control in the hands of non-workers;**

(3) **use public loans or "seller" financing as much as possible, but prepare for long delays in obtaining public loans.**

(4) **if the firm will not be initially profitable, use sales/leaseback agreements and limited partnerships to finance plant and equipment, research and development and advertising;**

(5) **to cover any financial gaps, workers will have to contribute their own savings, but should avoid using money they cannot afford to lose, particularly pension fund assets.**

Table 9

BALANCE SHEET FOR A MANUFACTURING FIRM

Total Assets	
Cash in hand and in banks	$ 323,929
U.S. Government and other securities	201,180
Total receivables	1,683,470
Inventories	1,968,313
Current assets, n.e.c.	277,678
Total current assets	$ 4,454,570
Net property, plant and equipment	3,654,710
Non-current assets not specified elsewhere, including investment in non-consolidated entity	1,890,720
Total Assets	$10,000,000
Liabilities and Stockholders Equity	
Short-term loans	$ 377,395
Trade accounts	984,290
Installment due in 1 year on long-term debt	111,460
Other current liabilities	1,204,104
Total current liabilities	$ 2,677,249
Long term debt	$ 1,663,481
Non-current liabilities, n.e.c.	674,402
Minority stockholders interest in consolidated corporations	20,358
Total Liabilities	$ 5,035,490
Capital Stock	1,269,967
Retained Earnings	3,694,543
Stockholders Equity	4,964,510
Total Liabilities & Stockholders Equity	$10,000,000

At The Rath Packing Company in Iowa, the union led the buyout effort and structured the company to assure worker involvement on all company levels.

APPENDIX I: RESOURCES FOR EMPLOYEE OWNERSHIP*

Initial Information and Referral

National Center for Employee Ownership 114 Sansome Street San Francisco, California 94104 (415) 788-7200 Catherine Squire, Regional Director	o California office of NCEO o Information materials o Technical assistance o Research o Free referrals to experts
National Center for Employee Ownership 4836 S. 28th Street Arlington, Virginia 22206 (703) 931-2757	o Information materials o Research o Free referrals to experts
California Economic Adjustment Team State of California Department of Economic and Business Department 1030 13th Street, Suite 200 Sacramento, California 95814 (916) 322-5665	o Technical assistance o Referrals to experts o Help locating funding sources
Plant Closures Project 433 Jefferson Oakland, California 94607 (415) 834-5656 Ellen Green, Coordinator	o Union church alliance to address problem of plant closures o Technical assistance o No cost referrals to experts
California Labor Federation AFL-CIO Research Department 995 Market Street San Francisco, California 94103 (415) 986-3585 Charles Jeszeck, Research Director	o No cost referrals to experts
Association for Workplace Democracy 1747 Connecticut Avenue, NW Washington, D.C. 20009 (202) 265-7727	o Loose network of individuals and local chapters

Technical Assistance

California Economic Adjustment Team State of California Department of Economic and Business Department 1030 13th Street, Suite 200 Sacramento, California 95814 (916) 322-5665	o Technical assistance o Referrals to experts o Help locating funding sources

* This list focuses on California resources. It is not a complete list, nor does it recommend any specific organization.

Technical Assistance (continued)

New Ways to Work 457 Kingsley Avenue Palo Alto, California 94301	o Technical assistance
Industrial Cooperative Association 249 Elm Street Somerville, Massachusetts 02144	o Technical assistance o Feasibility studies o Referrals to experts
National Economic Development & Law Center 2150 Shattuck Avenue #300 Berkeley, California 94704 (415) 548-2600	o Technical assistance o Legal and financial advice
Mid-Peninsula Conversion Project 867 West Dana #203 Mountain View, California 94041 (415) 968-8798	o Technical assistance for alternate use planning (conversion to alternative products)
Action Resources West 1218 S. 1200 West Salt Lake City, Utah 84104	o Technical assistance (worked with Rath, GM Hyatt Clark and National Steel)
Community Economics, Inc. 6529 Telegraph Avenue Oakland, California 94609 (415) 652-5100	o Financial and legal consulting
Menke & Associates 235 Montgomery Street, Suite 844 San Francisco, California 94104 (415) 392-0648	o ESOP lawyers
Commonwealth Group 601 California Street San Francisco, California 94104	o ESOP lawyers
Ludwig & Curtis 114 Sansome Street San Francisco, California 94104 (415) 788-7200	o ESOP lawyers

Legal Assistance

Deborah Groban Olson 1005 Parker, Suite 4 Detroit, Michigan 48214 (313) 331-7821	o Labor, civil rights and employee ownership attorney
Charles F. Bloodgood Bloodgood & Dwyer 1005 8th Street, Suite 403 Sacramento, California 95814	o Labor attorney o Co-operatives
Van Baldwin 2150 Shattuck Avenue #300 Berkeley, California 94704 (415) 548-2600	o Co-operatives
David Shore 901 H Street Sacramento, California 95814 (916) 448-1675	o Co-operatives
Stephen M. Tennis Ware, Fletcher & Freidenrich 525 University Palo Alto, California 94301 (415) 328-6561	o Co-operatives

Organizational Development

New School for Democratic Management 589 Howard Street San Francisco, California 94105 (415) 543-7973	o Education in democratic management and basic business principles for employee owners and others.
David Olsen 42 Winfield Street San Francisco, California 94110	o Quality of Working Life Guidance
Yates and Associates 170 Mapache Drive Portola Valley, California 94025 (415) 851-2690	o Counseling on organizational development

Business Schools

Stanford University Associate Dean of Master of Business Administration Program (415) 497-2836	o Faculty and students may prepare market or economic studies

Business Schools (continued)

UCLA
Dean of Master of Business Administration Program
(213) 825-4316

UC Berkeley
Associate Dean of Graduate School of Business
(415) 642-6000

San Jose State University
Director of Graduate Program of School of Business
(408) 277-2308

San Francisco State University
Dean of Graduate School of Business
(415) 469-2668

Financial Assistance

Sources of Capital Targeted to Worker Ownership

National Consumer Cooperative Bank
1330 Broadway, #1010
Oakland, California 94612
(415) 273-7576

Revolving Loan Fund
Industrial Cooperative Association
249 Elm Street
Somerville, Massachusetts 02144
(617) 628-7330

Affirmative Investments
Harvard Square, P.O. Box 801
Cambridge, Massachusetts 02238
(617) 491-0203

Other General Publications

Hayes, John and Smollen, Leonard, Sources of Capital for Community Economic Development. Cambridge: Center for Community Economic Development, 1976.

The Corporate Finance Source Book: 1982
Karen Zehring, Editor
available in libraries or from
40 Central Park South
New York, New York 10019

APPENDIX II: GUIDES AND BOOKS ON EMPLOYEE OWNERSHIP

Plant Closings: A Worker's Handbook
Prepared by the AFL-CIO
Great Lakes Regional Council
500 West Central Road, Suite 205-1
Mt. Prospect, Illinois 60056

A Guide for Communities Facing Major Layoffs or Plant Shutdowns
U.S. Department of Labor
Washington, D.C.
U.S. Printing Office, 1980

WE OWN IT: Starting and Managing Co-ops, Collectives, and Employee Owned Ventures
Bell Springs Publishing
P.O. Box 640
Laytonville, California 95454

How to Organize a Worker Buyout
Industrial Cooperative Association, Inc.

Financing Employee Ownership
National Center for Employee Ownership
Publication No. PG-1

Selling a Small Business to Its Employees Through an ESOP
National Center for Employee Ownership
Publication No. PG-2

History of Work Cooperation in America
John Curl
Homeward Press
P.O. Box 2307
Berkeley, California 94702

Unions and Employee Ownership
A Symposium
National Center for Employee Ownership

Organizing Production Cooperatives
William Alvarado-Greenwood
National Economic Development and Law Project, 1979

Determining the Economic Feasibility of a Cooperative
Cooperative Extension Service Circular No. 412
New Mexico State University
Los Cruces, New Mexico

"Strategies Against Shutdowns: A UAW Plant Closings Manual."
UAW Legal Department, February 1981

Employee Ownership: A Handbook
National Center for Employee Ownership, Publication No. BS-1

Annual Resource Guide (for employee ownership)
National Center for Employee Ownership, Publication No. BS-3

"What is a Worker's Cooperative?"
Industrial Cooperative Association

"Analysis of a Worker Buyout Attempt," 5 pgs.
Industrial Co-operative Association

"The Dangers of Worker Control."
The Nation, October 2, 1982

"Union Experiences With Worker Ownership: Legal and Practical Issues Raised by ESOPs, TRASOPs, Stock Purchase and Co-operatives" by Debra G. Olson, Wisconsin Law Review, 1982, page 853-946.

APPENDIX III: FILMS ON PLANT CLOSURES AND WORKER OWNERSHIP

Many of the following films can be rented from California Newsreel, 630 Natoma Street, San Francisco, California 94103, (415) 621-6196.

WORKER OWNERSHIP

Blue Collar Capitalism — Film, 1978, color, 30 minutes
Rental: Cornell University, (607) 256-4405

In April, 1975, Vermont asbestos miners bought their mine when it was to be closed by a conglomerate parent. This film shows key issues that arise when workers become owners.

Temescaming — 16 mm color, 1975, 64 minutes
Rental: California Newsreel, (415) 621-6196

In Canada, workers and local managers bought their paper mill from a U.S. corporation to avert closure. Essential viewing for workers and communities considering employee/community ownership.

The Mondragon Experiment — 16 mm color, 1981, 55 minutes
Rental: California Newsreel

Detailed look at the world's largest and most successful venture in worker ownership. Located in the Basque region of Spain, the Mondragon cooperative movement is a network of 65 enterprises with 15,000 worker members.

The Fight Against Black Monday — 16 mm color, 1978, 75 minutes
Rental: California Newsreel

Describes efforts by the Mahoning Valley Ecumenical Coalition to develop a plan for keeping the Youngstown Sheet & Tube steel mill open under worker community ownership in 1977.

Buyout — 16 mm color, 1982, 30 minutes
Rental: California Newsreel

This film poses the complex issues surrounding the buyout of an unprofitable GM parts plant in New Jersey by 1,200 workers and managers. Both groups compete to make production and investment decisions, while they also must work together to make the plant profitable.

APPENDIX III: FILMS ON PLANT CLOSURES AND WORKER OWNERSHIP (continued)

PLANT CLOSINGS/ECONOMIC DEVELOPMENT

It's Not Working — 16 mm color, 1980, 25 minutes
Rental: California Newsreel

Workers from a variety of industries discuss alternatives to plant closings, such as locally-owned co-operatives to make their reopened plants economically feasible.

What's Good for GM — 16 mm color, 1981, 45 minutes
Rental: California Newsreel

Investigates the trade-offs for the community in Detroit where the Poletown neighborhood was razed to make way for a new GM factory.

The Reckoning — 16 mm color, 1979, 26 minutes
Rental: California Newsreel

Professor Harvey Brenner of Johns Hopkins University presents fifteen years of research on the effects of unemployment on health.

We've Always Done It This Way — 16 mm color, 1979, 36 minutes
Rental: California Newsreel

This film describes the innovative efforts by Stewards at Lucas Aerospace, a British multinational defense contractor, to save jobs by developing an Alternative Corporate Plan. Stewards developed over 250 new products and marketing strategies, linking worker skills to existing social needs.

Shutdown — Videotape
Rental: United Auto Workers

Mad River: Hard Times in Humbolt County — 16 mm color, 1982, 54 minutes
Fine Line Productions
Box 315, Franklin Lakes, N.J. 07417
(201) 891-8240

A rural community in Northern California, critically dependent on the timber industry, seeks alternative economic solutions to mill closings an an unemployment rate twice the national average.

PLANT CLOSINGS/ECONOMIC DEVELOPMENT

The Business of America — Video, color, 1982, 45 minutes
Rental: California Newsreel

As basic American industry declines, plant shutdowns are leading workers and communities to consider buyouts, worker input into decisions, and other options. The film suggests that employees can participate not only in their daily work situations, but also in economic policy formation.

Planning Work: Resources on Technology and Investment for Labor Education
Available from: California Newsreel

Resource Manual for union input in planning for industrial change. The manual provides assistance to union planning concerning new technology, investment strategies and job redesign.

LABOR MANAGEMENT COOPERATIVE PROBLEM-SOLVING

Jamestown Documentary — 1/2" videotape, 1975, 60 minutes
Rental: Jamestown, NY, (716) 661-2262

Examines the efforts of the Area Labor Management Committee in Jamestown, New York, to identify problems and implement solutions to the decline of local industry.

APPENDIX IV: FACTS ON WORKER BUYOUTS

COMPANY (INDUSTRY)	NO. OF EMPLOYEES	UNION	GENERAL CHARACTERISTICS: DIVESTING COMPANY	GENERAL CHARACTERISTICS: WHY SOLD	GENERAL CHARACTERISTICS: DATE OF EMPLOYEE OWNERSHIP	FINANCING: COST OF BUYOUT
:hicago Northwestern Railroad	14,800 (5,798 owners)	railroad unions	Northwest Industries	Unprofitable	1972	$30 million
Vermont Asbestos Group (mining)	175		General Analine & Film Corp. (GAF)	Regulatory problems and pessimism over ore reserves	1975	$550,000 total capital $2.25 million
Saratoga Knitting Mill (lingerie maker)	70 originally increased to 180. (91 in 1982)	non-union	Cluet Peabody	Unprofitable under conglomerate ownership	1975	$730,000 ($390,000 guaranteed by SBA)
Okinite (wire & cable mfg.)	1,900 7 plants Santa Maria, CA plant has 125	Several unions	Omega-Alpha filed for bankruptcy in 1974	Parent company went bankrupt	1976	$44 million
South Bend Lathe (machine tool mfg.)	450 now 227	United Steel Workers of America Local 1722	Amsted Industries	Parent company wanted to divest - a buyer wasn't found	1975	$7.25 million
Mohawk Library Burea Ierkimer Library Bureau (furniture mfg.)	270	IUE Local 344	Sperry Rand	Product didn't fit with conglomerates overall plans	1976	$4.6 million
Colonial Cooperative Press	24		Sheller-Globe	Unprofitable	1978	No buyout
Rath Packing (meat products)	2,300 6 plants	UFCW Local 46	Rath issued stock	Marketing problems poorly managed	1979	$3.6 million (plus working capital)
Jeanette Glass (sheet glass)	340	United Glass and Ceramic Workers	Fourco Glass (AFG)	Parent didn't want to invest in new technology	1980	$4.8 million
Hyatt Clark Industries (bearings for cars)	750 now 1,100	UAW Local 736	General Motors	Lagging demand for product	1981	$55 million

FINANCING	OWNERSHIP		
FUNDING SOURCES	% OF EMPLOYEE STOCK & VOTING RIGHTS	EMPLOYEE REPRESENTATIVE ON B.O.D.	RESULTS
	75% emp. owned, no voting rights for 10 years		Profitable 8 of 9 years following buyout. Record 1981 earnings - $54.3 mil. Employee suggestion system produced 790 paid worker ideas.
$1.5 mi. VT. Industrial Dev. Authority loan $400,000 SBA loan $100,000 equity from employees & community	78% owned by workers and the community	Between 1975-78 BOD consisted of 7 wage earners 7 salaried 1 outsider	Financial success due to a 65% increase in price of asbestos; decreased equipment and maintenance costs. 19% increase in wages & benefits in first year. No longer employee owned.
$500,000 loan from business development corps & local bank $80,000 loan Job Development Authority $150,000 equity (41 managers and workers)	70% owned by employees, no voting rights for 15 years. 30% community owned	2 workers of 7 member B.O.D.	Turnover down. Absenteeism up. Waste down. $500,000 loss in year before buyout changes to $257,000 profit four years later. Half of the owners sold out because they felt lack of control. Running at 40% capacity in 1982. Diversifying products.
$13 million loan Economic Development Administration $31 mil. private loans	100% owned stock accrual based on salaries and seniority, no voting rights	New Jersey Bank is ESOP Trustee	$1.5 mil. of stock recently distributed to 230 retirees 290 employees at North Brunswick plant went on strike in 1980 arguing they had no control over stock. Continues to be profitable.
$5 mil. EDA loan $2.25 mil. private employees trade 80¢/hr & pension plan for stock	By 1981 67% owned by employees but only 22% vested & voting stock based on salary	Union President on B.O.D.	Rejects down. Profitable company. Survey after 18 mos. - employees and management said company changed for better; 180 of 450 workers signed petition in 1977 demanding 50% representation on B.O.D. Nine week strike in 1980.
$2 mil. EDA loan $1 mil. local banks $1.5 mil. worker & community equity	30% employee owned, non-voting stock. In 1981 a local businessman bought 51%	1979 union declined seat on B.O.D.	Survey 1 year after buyout showed improved communications, pride in product. Losses in 1977 and 1978 due to low bidding and expansion.
New corp. started $260,000 Mass. Community Development Finance Corp. $30,000 MA Office of Communities & Development $25,000 workers	100% voting stock	All (?)	Buyout failed, 30 workers started new firm which later failed.
$3.6 mil. deferred earnings & benefits $3 mil. EDA loan $4.5 mil. UDAG loan $5.1 mil. deferrals	60% voting stock	12 workers reps on 17 member B.O.D.	Action Resources West is consultant. A survey one year after the buyout showed improved attitudes. Company unprofitable for many years before conversion; mixed since then.
$700,000 equity from workers $720,000 loan from PA Ind. Dev. Auth. $2.8 mil. bank loans ($600,000 AFG note)	Management controlled trust (designed by union's lawyer) stock allocated by salary	6 member B.O.D. 4 workers	Workers exchanged their pensions for ESOP. Company currently profitable. Producing 15% more glass with fewer employees. Company was profitable and in today's market is breaking even.
$30 mil. bank loans $20 mil. G.M. loan & preferred stock employees defer wages which were $13.50 hr. & now are $10.40	In 10 yrs. it will be 100% employee owned	3 selected by union, 3 selected by mgmt., 7 selected by both ultimately, the union will appoint half the B.O.D.	Plant is now competitive according to new president. Quality has improved. Reduced utility bills. Gain-sharing plan. Executive "perks" were reduced. Company is working to develop a new product to replace their current one during the next 10 years.

APPENDIX V: ORGANIZING A BUYOUT COMMITTEE AND TASK FORCES: WHAT TO DO AND HOW TO DO IT

Transferring ownership is a complex process which can involve many interest groups from the community. To obtain support and cooperation of divergent and necessary interest groups, you need to organize and develop a plan everyone agrees on.

The necessary steps are described below:

1. **Identify influential people in the union, management and the local political system.**

2. **Put together a Buyout or Community Response Committee.**
   Members could come from:

   Local Community Representatives
   City/County Government
   Private Industry Council
   Social Service Agencies
   Church
   Banks and Financial Institutions
   Educational Institutions
   Economic Development Agencies
   EDD Field Office

3. Once the committee is organized, specific activities can be identified. Resources can be mobilized within the firm, in the community and at the state level to examine alternatives to the closure.

4. Form Task Forces to deal with the following issues. Several issues can be dealt with by a single team if that makes sense.

   a. **Deal with management regarding what is behind the closure, ways to avoid closure, what are options.**

   b. **Effects of Closure: On employment, tax base, etc.**

   c. **Education For All Groups: Workers, managers, staff.**

   d. **Community Support: Town meetings, meet with politicians.**

   e. **Marketing: Is there a market?**

   f. **Plant Economics: Can your plant compete in the market?**

   g. **Financial Options: Workers put in money, deferred benefits, loans, state funds, ways to raise money, getting money out.**

   h. **Legal Options: ESOP/Co-op structure, who controls company?**

   i. **Tax Options: How to minimize costs and structure company.**

   j. **Labor Management Cooperation: In a newly employee owned facility this issue is easily skipped and problems result.**

Management Liaison

If appropriate, **discuss with management of the firm what is behind the plant closing, ways to avoid the closure, and what are the options.** Questions concerning what is behind the closure are as follows:

1. Why specifically is the company closing the plant?

   - Transportation costs for new materials
   - Transportation costs for finished product
   - Quality of the workforce (costs, productivity, local labor force availability)
   - Plant is not a good fit with conglomerate parent:
     e.g. conglomerate wants to divest a plant or division
     e.g. plant doesn't earn the desired rate of return
     e.g. conglomerate management isn't equipped to manage the local company
   - Market demand
   - Age of plant
   - Capital scarcity
   - Regulations
   - Related suppliers
   - Taxes

2. Will the production capacity be transferred elsewhere?

   - How much will be transferred
   - What product lines
   - Where will each product be produced

3. How much will the company add to the labor force in these locations?

4. Could you provide a complete list of your related plants with the following information:

   - Location
   - Capacity: Amounts, types, potential (full capacity)
   - Whether open or closed

A positive relationship and interaction with the owner can provide potential advantages:

- A fair selling price should employees choose to buy the company or plant
- Access to company books
- Assistance of managers in assessing company viability
- Loans and other financial assistance
- Technical and administrative support
- Cooperative marketing arrangements

Information on companies can also be obtained from:

Data Center
464 19th Street
Oakland, CA 94612
(415) 835-4692

- Up-to-date corporate profiles on over 100 companies.
- Research service relevant to specific requests.
- Clipping service on plant shutdowns, steel and other topics.

Corporate Data Exchange
198 Broadway
New York, New York
(212) 962-2980

- Corporate data, focusing on stock ownership.

Effects of the Closure

Usually in potential closure situations, the county tax assessor determines effects of the closure on the tax base. **Broad local support can be generated by a full understanding of the total costs of the plant closing.** A rudimentory list of potential effects of closures that the employees should try to identify is listed below:

Losses to the Community

Employees can determine these immediate effects of the closure by contacting the city treasurer and county tax assessor:

- o Property tax paid by the company on plant, equipment and land (real property and personal property tax)

- o Utility taxes paid by the company

- o Income taxes paid on the company local payroll

Other community losses which should be recognized are:

- o Sales taxes paid on supplies purchased by the company

- o Consumption power is reduced since unemployment insurance provides less income than workers earned prior to the closure (e.g. $221,000 lost in 26 weeks for a 100 person plant; estimate State of New Jersey, Dept. of Labor)

  Employee property taxes as homes are devalued.

  "Ripple effect" which includes losses such as the above to other firms which purchase from or sell to the closing plant.

  Underutilized infrastructure resulting in lost fees for public utilities.

At the same time that the community tax base is reduced, needs of social services increase. Costs to the community and state include:

- o Unemployment compensation (administrative costs)

- o Welfare benefits

- o Food stamps (administrative costs)

- o Increased social service costs (crime prevention, mental health, Medi-Cal and County Hospitals)

Public Information and Mobilization: Educating All Employees and Community

Membership in a task force to educate people should include influential people in the union who can coordinate worker education, and, if possible, middle management. Key representatives of the union, financial institutions, business and government can mobilize other community support.

The key activities of such a task force include the following:

I. Worker/Employee/Community Education Meeting

Most transfers of ownership include at least one public education meeting for the community and employees. The public meeting is one mechanism to assess support and obtain funding for the initial viability assessment and other technical assistance. The education meeting informs interested people of the buyout option and the organization necessary to achieve it. The meeting also helps mobilize support. Key questions which the meeting should answer are:

- o What is employee ownership?
- o Will it work?
- o What happens once employees own the firm? (Film--see Appendix for examples)
- o What key steps or actions need to occur next?

II. Political Liaison Activity

Active political support is often critical to the successful transfer of ownership. At Rath, local political leaders helped convince management to accept the workers' offer and assisted the group in securing federal monies. At VAG, the active involvement of Vermont's governor, the state legislature and area congressmen was essential in the effort. A state agency also financed a feasibility study and provided loan guarantees. In the Continental Airlines effort key legislators in California were involved. Key people and their potential contributions are described below:

- o Government and political leaders can assist in negotiations with management and can unite the community behind the job preservation effort.

- o State agencies can finance feasibility studies, provide loan guarantees.

- o Political representatives can mobilize community financial support. Political support can also assist in obtaining government funding from UDAG, SBA, FmHa, EDA.

- o In some cases, local business groups have mobilized support for the workers. Small businesses in a community have much to lose if a major firm closes, in loss of purchasing power, decline of services and loss of population in the area if workers move.

- Churches and other social agencies have the potential for playing a major role in organizing the community.

- Most importantly, grassroots support is critical, especially in worker/community ownership. In the case of VAG, community mobilization resulted in raising $1.5 million for the buyout. In Herkimer, workers and volunteers sold stock like raffle tickets and raised $1.8 million.

III. Worker/Education

It is critical to make information available to all interested parties throughout the buyout process. After the initial introductory meeting, subsequent meetings should be held as often as necessary. Employees want to be informed of events and decisions regarding worker ownership. Check whether:

- Union meetings include discussion of employee ownership.

- The union newspaper provides timely, relevant information.

- The company newsletter includes information so that supervisors and management remain informed.

- Workers can form an in-plant committee of representatives to inform workers in their individual departments of events and decisions regarding worker ownership.

- Stewards and other union representatives disseminate information.

- Supervisors can be valuable to answer questions and provide information.

IV. Media Support: Information helps build public support.

- A list of media contacts helps reduce time in disseminating press releases and scheduling press conferences.

- Press releases or written information to provide to media representatives helps assure accurate reporting regarding the employee buyout. Interviews and informal comments can be misinterpreted or taken out of context.

V. Union Involvement in the Buyout

Make sure employees understand these key considerations:

1. Interest differences can exist between the international union and the local.

   Local union officers concentrate their energy on maintaining jobs, good benefits and working conditions. While top union officials share these objectives, they are also concerned with maintaining the standards won in the past in company-wide or industry-wide master agreements.

Employee ownership plans have sometimes involved some form of benefit reduction. In the more recent cases where employees have reduced benefits and bought stock, careful structuring of the agreement has permitted workers and the local union to remain in the master agreement. If stock and increased influence are exchanged for benefits, the local can remain symbolically in the master agreement.

Union locals may increasingly work with their international unions to structure worker ownership to protect members in sister plants.

2. Worker risk is a significant concern. Worker ownership can be structured so that workers minimize the risks of ownership. In many cases, buyouts use a leveraged ESOP, in which workers become owners of stock paid for out of future earnings of their company. James Smith, Assistant to the President of the United Steelworkers of America, notes that "employee stock ownership plans should occur only in addition to an adequate, funded pension plan." If the local union believes that giving up the pension is necessary to save jobs, alternatives exist for union consideration. The union can propose that union and management jointly study the company costs in hope of determining ways to resolve the employee owned company's financial problems without sacrificing the pension. If this joint study indicates poor prospects for company survival if the pension plan is unchanged, the union can negotiate changes in the plan while protecting long-term employees.

Marketing, Plant Economics, and Financing Options

Because market and plant economics are both part of the economic feasibility study, in most cases they will be evaluated together. The important role of an economic feasibility team will be to:

(1) locate experts to do the feasibility study;

(2) find a means to pay for it (or negotiate free services);

(3) watch over the performance of the feasibility study.

In an optimal situation, someone on the team will be familiar with the firm's finances and operations. Suggestions for how to complete the tasks described here are provided in the two sections on the feasibility study.

While the feasibility study is being completed, financing options should be lined up. The economic feasibility team should begin to make contacts with state and federal agencies and private financial institutions, and find out what their programs require. It should also seek out other individuals and organizations that might have an interest in providing capital to the employees, including local investors.

Legal Issues: Ownership Structure and Tax Options

There are many varieties of employee ownership. Both employers and workers can benefit from the use of some of these methods. **Some workers and unions have been hurt and disappointed, however, by the results of employee ownership. The structure initially established for the new company affects the firm in the future.**

Knowledge and planning are key to making wise choices in this area.

Competent legal advice is necessary on ownership structure. This can come from a local attorney with the assistance of an ESOP/co-op attorney. The National Center for Employee Ownership (703/979-2375) can provide interested parties with a list of available attorneys with experience and expertise in employee ownership. Costs can be reduced by using model documents as a guide for your attorney. Model ESOP and co-op incorporation and by-law documents are available from:

I.C.A.
249 Elm Street
Somerville, MA 02144
Co-op by-laws/incorporation
price: $25.00

N.C.E.O
4836 S. 28th Street
Arlington, VA 22206
Model ESOP
price: $75.00

Key issues and questions include the following:*

Ownership

What portion of the stock will employees purchase?

- o Partial ownership: Stock can be an employee benefit. In collective bargaining with a company which says it cannot afford to increase wages or benefits, stock ownership can be an additional benefit. If given through an ESOP or PAYSOP, it gives considerable tax advantages for the employer and deferred retirement income for workers.

- o Majority ownership: Ownership brings a bundle of rights and responsibilities, if long-range planning can assure an agreed upon structure. Organizing and controlling the voting shares can give a union bargaining power over subjects which it cannot require the employer to discuss in collective bargaining.

Share Allocation

Share allocation can be based on:

- o Wages/salary - this favors the most highly paid employees in the company.
- o Hours worked since plan initiation.
- o Seniority - favoring longest term employees.

* ESOP legal issues are taken from Attorney D. Groban Olson's excellent summary "Legal and Practical Considerations for Unions about Negotiating Employee Ownership Benefits and Worker Buyouts" (listed on page 54).

- o Equal allocation to all employees provides democratic ownership. (A co-op ESOP is one that obtains 100% of the employer's stock or at least a controlling interest and each employee gets an equal share. The firm gets the tax advantages of an ESOP while assuring cooperative structure and collective control over the majority interest.)

Voting Rights

Voting rights must be a key area of concern and careful planning for any union considering an ESOP. Voting rights for all workers are also important issues for co-ops.

- o PAYSOPs must and ESOPs can pass through voting rights. Public trade companies must pass through voting rights on all corporate issues; closely held companies must pass through the vote only on major issues, like mergers and liquidation.

- o One person one vote provides for a democratic structure.

- o Employees may be offered straight stock purchase plans.

- o There are different classes of stock. Preferred stock usually has a guaranteed dividend and no voting rights, while common stock has voting rights but no guaranteed dividend.

- o There are different classes of common stock, with different types of voting rights, including some common stock with no voting rights. There are arrangements in which for instance, 10% of the common stock is Class A, but Class A stock controls six out of ten seats on the board of directors while 90% of the stock is Class B, which controls four out of ten seats on the board.

- o There are more safeguards for voting rights on ESOP stock acquired since December 31, 1979.

Vesting Provisions

Vesting refers to the percentage of an employee's account balance in the ESOP which is non-forfeitable at the time that the employee leaves the plan. The law requires that the plan choose a schedule at least as favorable as one of the following schedules:

- o 100% vesting after ten years.

- o 25% vesting after five years of service, increased by 5% in each of the next five years, and by 10% in each of the following five years, thus reaching 100% after fifteen years.

- o 50% vesting after ten years, increased by 10% annually thereafter, with more rapid vesting in favor of employees over the age of about 35.

The ESOP Trustees

- The ESOP is administered by a committee which instructs the trustee on voting ESOP stock and other administrative duties. The trustees can be appointed by:

  - the employer or management
  - management and the union
  - democratic election by plan participants

- Trustees can be union representatives or specific restrictions can assure that trustees are not an officer, employee or agent of the union.

- How many trustees will there be?

- How often will the trustees be nominated and elected?

- Are there representatives on the Board of Trustees from all employee owners or are some groups not represented?

The Board of Directors

The board of directors sets company policy and practice. It also monitors and evaluates corporate executive action to implement policy and administer the company.

- What is the desired number of worker/employee representatives on the board?

- Are all seats elected directly by the stockholders? If yes, the majority voting bloc can elect all the directors. If no, a non-majority bloc can at least gain director seats.

- Potential problems encountered elsewhere by worker directors include:

  - lack of previous experience
  - insufficient training
  - problems of dual loyalty
  - compulsory worker representatives could be resented by management board members
  - no clear union policy regarding union directors

The Pension Plan

Where there is an existing pension plan, an ESOP can be created in addition to the existing pension plan. Capital needed for the buyout should not come from the pension plan. The ESOP may be able to borrow money. Employees may regularly buy stock by payroll deduction. In some cases employees have lost pension benefits which could have become vested had the plan changes been fully understood and negotiated.

If a tax qualified pension plan is converted to an ESOP, possible effects include:

- o Assets of pension plan may be invested in employer securities in amounts greater than the 10% allowed by ERISA.
- o The employer may avoid additional vesting.
- o If the plan is terminated the rights of all affected employees to benefits accrued, to extent they are funded, become vested.
- o If the pension plan is terminated, the Pension Benefit Guarantee Corporation (PBGC) becomes involved. The PBGC can obtain up to 30% of company assets to meet the plan's obligations to beneficiaries. Such a lien could force a company into bankruptcy or closure.
- o ESOP benefits are not guaranteed by the PBGC.

Employee Community Ownership

Key issues in structuring employee community ownership focus on the amount of control over the firm that the employees and community have. This includes percentage of ownership by the two groups, whether or not employee stock is held in a trust and voted as a bloc, and the representation of all groups on the board of directors. Participants must decide whether or not stock can be sold to outsiders and if desired, mechanisms should be established to maintain local control of the firm. "Community" is also difficult to define and can lead to control by a few local business interests.

Co-operatives

A co-operative may be established within the shell of a for profit corporation or as a non-profit, non-stock corporation.

Co-op/ESOP

An ESOP/Co-op combines the advantages of the ESOP with the co-operative form of organization. This includes patronage dividends paid to co-op members to increase their immediate incomes and company contributions to an ESOP with tax benefits for the company and employees. For further information contact Norman Kurland, Attorney, 4318 N. 31st Street, Arlington, Virginia 22207, (703) 243-5155, or Deborah G. Olson, 1005 Parker Suite 4, Detroit, Michigan 48214, (313) 331-7821.

PAYSOPS

A PAYSOP is a qualified employee benefit plan similar to an ESOP. Contributions to a PAYSOP, however, are eligible for a tax credit, rather than merely a tax deduction. The amount of stock workers receive from PAYSOPs is quite small, thus it would be used to augment tax advantages rather than to purchase a company. A PAYSOP can be a good experiment with the ESOP concept for a union interested in a small stock benefit plan keeping open future expansion options.

Labor Management Cooperative Problem Solving

All parties in a newly employee owned facility can benefit from labor management cooperation. Nevertheless, plans for labor management cooperation are easily skipped, leading to long-term problem ranging from dissatisfaction to declining profits.

Joint problem-solving provides workers with a way to share insights and make contributions to solving problems which affect job security, productivity, and work satisfaction.

Management also benefits from cooperative problem solving. Joint committees allow management to demonstrate its willingness to tackle worker concerns and follow through on constructive suggestions to improve work. Management can tap worker know-how and ingenuity.

Union benefits and risks include:

Benefits

- o Higher visibility
- o Increased representation, with which to address employee needs
- o Reduced cost of contract administration, grievances, arbitration
- o Access to information, prenotification of changes
- o Good public relations
- o Save jobs

Risks

- o More difficult role definition: management or union
- o Weakened union power
- o Greater liability for decisions
- o Intra-union splits
- o Negative rank and file perception
- o Job losses resulting from productivity increases

The steps to follow in establishing labor management cooperation are as follows:

1. Begin with the Steering Committee made up of equal representation of local labor and management. The committee should have labor and management co-chairs and representatives from both top management and top union.

   - o Equal number
   - o Equal voice
   - o Equal authority, i.e. top management - top local union
   - o Labor and management are co-chairs
   - o Have scheduled meetings
   - o Distribute the agenda in advance

2. Third party facilitators, trained consultants who serve at the invitation of the joint committee, can help overcome problems. This most basic function is to enhance mutual trust between labor and management. If one is hired:

   - o Who will pay them?
   - o Who do they answer to?
   - o Will they train internal people?

3. Make a charter to clarify aims and goals, to define structure and boundary conditions. Unions usually include safeguards either in the charter or in the contract.

   - Labor management cooperative activity will not violate the collective bargaining contract or grievance procedure
   - Job security for employees and management, i.e. no person will be laid off as a result of labor management cooperative problem-solving
   - Workers share increased productivity according to a jointly determined method

4. The basic concept of labor management cooperation included in the charter is that:

   > "There are many issues of concern that can be addressed through cooperative action...workers deserve to be included in decisions which affect both the quality of their work and the quality of their working life."

5. The agreement to organize a joint committee should be well publicized before the first meeting is held so that employees and management know what the committee is and what they can expect from it.

6. Joint problem-solving usually involves these basic steps:

   - Step 1: Identify problems and analyze causes.
   - Step 2: Brainstorm solutions.
   - Step 3: Evaluate solutions.
   - Step 4: Action planning.
   - Step 5: Follow through and communicate.

7. Most cooperative problem-solving programs are multi-tiered. A top group made of top labor/management representatives coordinates all committees and sets up new groups upon request. Department level groups are made up of labor and management working together to identify problems, find causes and solutions. This cooperative activity creates a parallel structure in addition to that of management and union. This is illustrated by the Rath example, shown in Table 10.

8. Training is necessary in employee ownership and joint problem-solving. The attitudes and skills that help people solve problems cooperatively do not always come naturally. One of the important functions of the third-party consultant is to help the union and management train participants.

9. Communication is extremely important to keep employees fully informed of all labor management programs. This will build confidence and reduce suspicion of "behind the scenes" collaboration.

   - Bulletin boards
   - Problem-solving groups
   - Union meetings and newspaper

10. An initial provision should be access to company data. Sharing of information is important to the success of joint labor management participation programs.

11. Employee ownership can permit greater input into decisions at various levels of the company. Plant-wide labor management committees deal with larger issues such as new product development, investment, reducing costs, absenteeism, etc.

- Depending on the level at which participation occurs, there are differences in the range of issues which can be discussed in joint problem-solving. The participation forms at each level are:

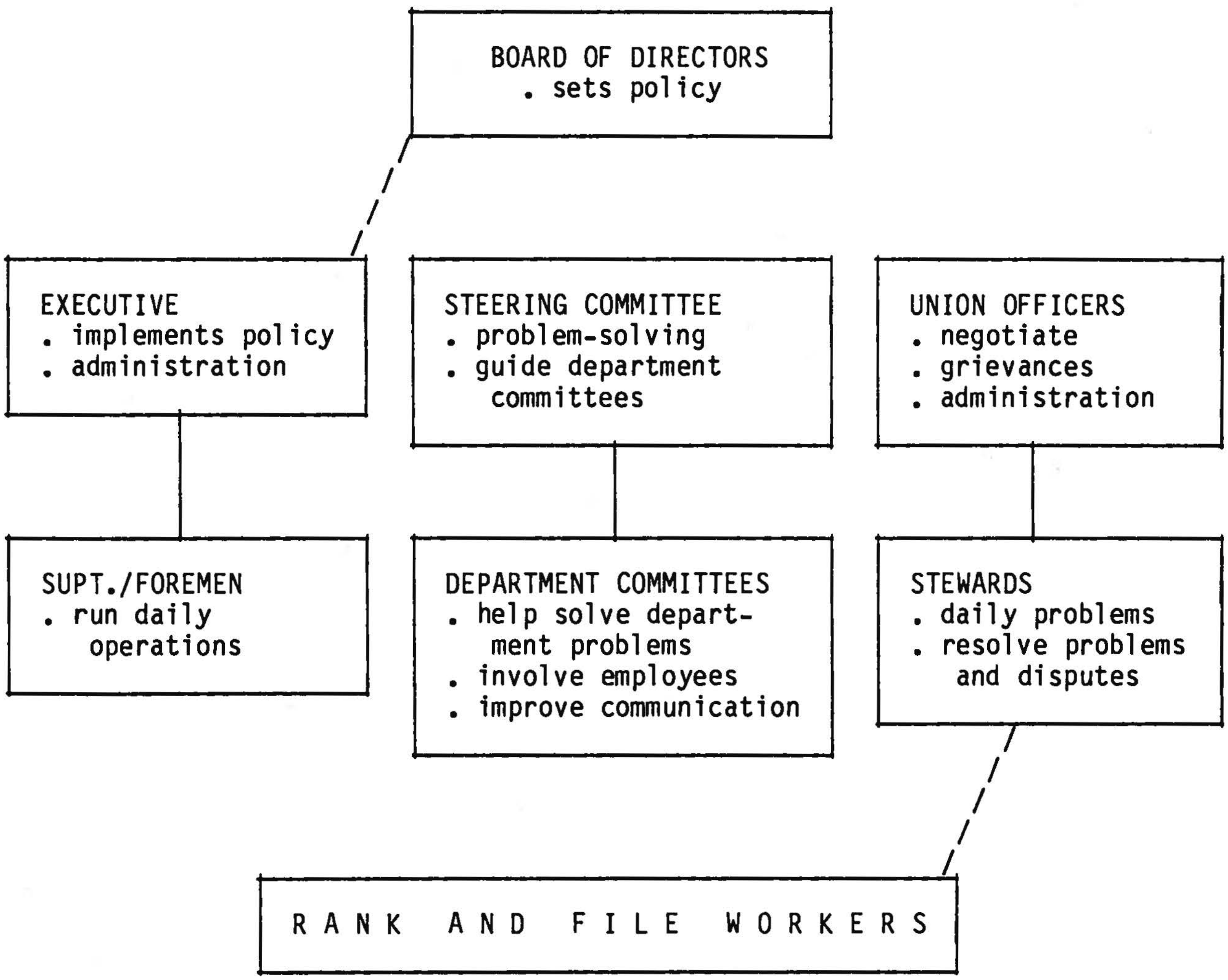
Level	Participation Form
Board of Directors	Representatives on BOD
Upper management	Collective bargaining/top management
Middle management/ plant level	Scanlon plans/steering committee
Dept./supervisor	Labor management committees
Shop floor	Shop floor participation Self-managing teams

Table 10

RATH PACKING COMPANY

PARALLEL STRUCTURE

In addition to the traditional union and management structures in the company, Rath's employee owners created a parallel structure for cooperative problem-solving. Union officers continue to negotiate, stewards handle daily problems, supervisors coordinate daily production. In addition, through labor management committees (LMCs), labor and management work jointly to solve issues of mutual concern.



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